No. 73-____

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MICHAEL RODAK, JR., CLERK

73-152

IN THE

Supreme Court of the United States

October Term, 1973

THE FIRST BOSTON CORPORATION,
Petitioner,

v.

CHRIS-CRAFT INDUSTRIES, INC.,
Respondent.

73-153

BANGOR PUNTA CORPORATION, NICOLAS M. SALGO AND DAVID W. WALLACE,
Petitioners,

v.

CHRIS-CRAFT INDUSTRIES, INC.,
Respondent.

73-154

HOWARD PIPER, THOMAS F. PIPER AND WILLIAM T. PIPER, JR.,
Petitioners,

v.

CHRIS-CRAFT INDUSTRIES, INC.,
Respondent.

JOINT APPENDICES TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

Counsel listed on First Page.

JOHN F. ARNING
CHARLES W. SULLIVAN
48 Wall Street,
New York, New York 10005.
Counsel for Petitioner
The First Boston Corporation

SULLIVAN & CROMWELL,
Of Counsel.

JAMES V. RYAN
C. KENNETH SHANK, JR.
One Rockefeller Plaza,
New York, New York 10020.
Counsel for Petitioners
Bangor Punta Corporation,
Nicolas M. Salgo and
David W. Wallace

WEBSTER SHEFFIELD FLEISCHMANN
HITCHCOCK & BROOKFIELD,
Of Counsel.

PAUL G. PENNOYER, JR.
EDWARD C. McLEAN, JR.
ZACHARY SHIMER
25 Broadway,
New York, New York 10004.
Counsel for Petitioners
Howard Piper, Thomas F. Piper
and William T. Piper, Jr.

CHADBOURNE PARKE
WHITESIDE & WOLFF
Of Counsel.

July 20, 1973.

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APPENDIX A

Opinion of Judge Charles H. Tenney of the United States District Court of the Southern District of New York in *Chris-Craft Industries, Inc.* v. *Piper Aircraft Corporation et al.*, dated August 19, 1969

Judge Tenney's Opinion

CHRIS-CRAFT INDUSTRIES, INC.,
Plaintiff,

v.

PIPER AIRCRAFT CORPORATION
et al., Defendants.

No. 69 Civ. 2227.

United States District Court
S. D. New York.
Aug. 19, 1969.

Paul, Weiss, Goldberg, Rifkind, Wharton & Garrison, New York City, Arthur L. Liman, Sidney S. Rosdeitcher, Joseph J. Ackell, Alan L. Schlosser, New York City, of counsel, for plaintiff.

Chadbourne, Parke, Whiteside & Wolff, New York City, Donald L. Deming, Richard B. Leather, Zachary Shimer, New York City, of counsel, for defendant Piper Aircraft Corp. and individually named members of Piper family.

Webster, Sheffield, Fleischmann, Hitchcock & Brookfield, New York City, James V. Ryan, New York City, William L. D. Barrett, Nancy Pasley, of counsel, for Bangor-Punta Corp.

OPINION

TENNEY, District Judge.

The instant suit arises out of the protracted and often bitter contest between plaintiff Chris-Craft Industries, Inc. (hereinafter referred to as "Chris-Craft") and defendant

Judge Tenney's Opinion

Bangor Punta Corporation (hereinafter referred to as "Bangor Punta") to gain control of defendant Piper Aircraft Corporation (hereinafter referred to as "Piper"). Alleging various violations by defendants of the Securities Act of 1933 and the Securities Exchange Act of 1934 and the Rules promulgated with respect to each such Act, Chris-Craft seeks an injunction *pendente lite* restraining Bangor Punta from: (1) accepting 107,574 shares of Piper common stock tendered by the public shareholders of Piper to Bangor Punta pursuant to the terms of Bangor Punta's General Exchange Offer of July 18, 1969. Chris-Craft urges that these shareholders be given the opportunity to rescind their tenders after a "full and fair disclosure" has been made of the terms of Bangor Punta's exchange offer; (2) acquiring additional shares of Piper; (3) effecting a merger or consolidation of Bangor Punta and Piper; and (4) voting 120,200 shares of Piper purchased in May 1969 by Bangor Punta in five large cash transactions, effected neither on a securities exchange nor from or through a broker or dealer.

Piper is a publicly-held Pennsylvania corporation whose capital stock consists of 5,000,000 authorized shares of $1.00 par value common stock, of which approximately 1,641,890 shares are issued and outstanding. The Piper family, three of whom are members of Piper's Board of Directors and defendants herein, own approximately 501,090 of the 1,641,890 outstanding shares. Piper's stock has been listed on the New York Stock Exchange (hereinafter referred to as "the Exchange") since 1957.

Chris-Craft is a diversified manufacturer whose common and preferred stock and convertible debentures are traded on the Exchange. Bangor Punta is a publicly-held diversified corporation whose stock and bonds are also listed on the Exchange.

Judge Tenney's Opinion

In January 1969 Chris-Craft, in an effort to gain control of Piper, began acquiring shares of Piper on the open market. On January 23, 1969, Chris-Craft publicly announced its interest in Piper and made a public tender offer for up to 300,000 shares of Piper stock at $65.00 per share with the "right to purchase excess shares."

Piper's Board of Directors, by letter dated January 27, 1969, advised Piper stockholders that in their opinion Chris-Craft's offer was inadequate and not in the best interests of Piper shareholders. Unsatisfied with the history of Chris-Craft's management, Piper's management and Board of Directors decided that the best interests of Piper and its shareholders required them to resist this attempted takeover.

On January 30, 1969, the Board of Directors of Piper and the Grumman Aircraft Engineering Corporation (hereinafter referred to as "Grumman") approved an agreement whereby Piper would sell 300,000 of its authorized but unissued shares to Grumman for $65.00 per share, in contemplation of thereafter exploring the possibility of a merger with Grumman. This agreement, although never realized, adversely affected Chris-Craft's cash tender offer, which expired on February 3, 1969.

On February 27, 1969, Chris-Craft filed a proposed registration statement and prospectus with the Securities and Exchange Commission (hereinafter referred to as "the SEC") in which it proposed to offer to exchange certain Chris-Craft securities for up to 300,000 shares of Piper.

Pursuant to its continuing efforts, on March 24, 1969 Piper issued 320,000 shares of its authorized but unissued common stock in exchange for all the outstanding stock of the United States Concrete Pipe Company of Florida, a subsidiary of a publicly-held investment company listed

on the Exchange. At the same time, Piper exchanged 149,199 shares of its authorized but unissued common stock for approximately 99½ percent of the outstanding shares of Southply, Inc., a closely-held Louisiana corporation. The Board of Governors of the Exchange, with whom listing applications covering the issued shares were filed, felt that the distribution of almost 30 percent of Piper's authorized stock violated the Exchange's listing criteria. Accordingly, trading in Piper stock was suspended and delisting proceedings authorized. When Piper's management agreed to rescind these transactions, trading in Piper stock was resumed.

While Piper's prolonged efforts to fend off Chris-Craft raise serious questions as to the propriety of such conduct, this action has little relevance to the instant proceedings. For the issues raised herein relate solely to Bangor Punta's exchange offer of July 18, 1969 and its purchases, for cash, of Piper stock in May 1969.

In early January 1969, defendant First Boston Corporation (hereinafter referred to as "First Boston"), an investment banking firm which serves as financial adviser to Piper, inquired whether Bangor Punta was interested in a possible acquisition of Piper. Although Bangor Punta responded affirmatively, nothing developed at that time. At a meeting convened on February 24, 1969, Bangor Punta explained that it would not consider attempting such an acquisition unless the Piper family sold their 501,090 shares to Bangor Punta. This condition was finally accepted by the Piper family on April 22, 1969.

On May 7, 1969, Chris-Craft publicly announced the terms of its then pending registration statement which proposed an exchange offer of Chris-Craft stock for 300,000 to 400,000 shares of Piper. The following day, after pro-

tracted discussions with Piper's representatives, a final agreement was entered into pursuant to which the Piper family agreed to exchange their shares for *specified* Bangor Punta securities. Additionally, the agreement provided that Bangor Punta would use its best efforts to acquire more than 50 percent of the outstanding shares of Piper stock. As part of those best efforts, Bangor Punta agreed to make an exchange offer to all other holders of Piper stock "under which such holders will be entitled to exchange each share of Piper common stock held by them for Bangor Punta securities and/or cash having a value, in the written opinion of The First Boston Corporation, of $80 or more." The agreement further provided that if Bangor Punta succeeded in acquiring more than 50 percent of the outstanding Piper shares, and if, in the written opinion of First Boston, the value of the shares offered to the members of the Piper family was less than $80.00 on the opening day of the exchange offer, Bangor Punta would deliver to the members of the Piper family securities and/or cash with a value "equal to the difference between $80 and the Exchange Offer Value." No agreement had been reached at that time as to the components of the proposed package of Bangor Punta securities to be offered to the public Piper shareholders.

Later that same day, Bangor Punta and Piper issued identical press releases announcing that they had reached an agreement under which Bangor Punta would acquire the Piper family's interest in Piper and that:

> "Bangor Punta has agreed to file a registration statement with the SEC covering a proposed exchange offer for any and all of the remaining outstanding shares of Piper Aircraft for a package of Bangor Punta securities to be valued in the judgment of the First Boston Corporation at not less than $80 per Piper share."

At that time, Piper stock was selling on the Exchange at approximately sixty dollars.[1]

On May 26, 1969, the SEC instituted an action against Bangor Punta and Piper in the United States District Court for the District of Columbia. Therein, the SEC charged that the May 8th press release was "gun-jumping" in violation of Section 5(c) of the Securities Act of 1933, as amended, 15 U.S.C. § 77e(c),[2] and SEC rule 135. Without admitting any of the allegations of the complaint, Bangor Punta and Piper consented to the entry of a final judgment of permanent injunction which enjoined them, *inter alia*, from offering to sell or from selling either of their securities until a registration statement was filed with the SEC as to such securities.

Bangor Punta filed its registration statement with the SEC covering its exchange offer on May 29, 1969. Included in the filing, as an exhibit to the registration statement, was a copy of the agreement of May 8, 1969. Preliminary prospectuses in the form contained in the registration statement were sent by Bangor Punta to all Piper shareholders of record on the same day the registration statement was filed. It became effective on July 18, 1969 and expired on July 29, 1969.

Bangor Punta now owns 728,864 shares of Piper, or 44.4 percent of its outstanding stock. As a result of its

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[1] Affidavit of John E. Flick, dated August 4, 1969, at 10.

[2] Section 5(c) of the Securities Act of 1933, as amended, 15 U.S.C. § 77e(c), provides:

> "It shall be unlawful for any person, directly or indirectly * * * to offer to sell or offer to buy through the use or medium of any prospectus or otherwise any security, unless a registration statement has been filed as to such security * * *."

most recent exchange offer, which terminated on August 4, 1969, Chris-Craft has now acquired a total of at least 654,000 shares of Piper, or approximately 39.8 percent of its outstanding shares. With approximately 259,026 shares of Piper still in the hands of the public, it would appear that at this time neither Chris-Craft nor Bangor Punta has succeeded in gaining control of Piper.

[1] Chris-Craft argues that the May 8th identical press releases of Bangor Punta and Piper constituted flagrant violations of Section 5(c) of the Securities Act of 1933, as amended, 15 U.S.C. § 77e(c) and SEC Rule 135, 17 C.F.R. § 230.135, in that no registration statement had been filed with the SEC prior thereto.

Until the actual execution of the May 8th agreement, only top management personnel and their confidential advisors had been advised of the negotiations with Piper. Upon execution, however, it became necessary to involve a great many other persons in the arrangements, such as an indenture trustee, independent auditors, printers, outside counsel and stenographers. Maintenance of security against premature disclosure of the terms of agreement became virtually impossible.[3] Since the $80.00 figure set by the terms of the agreement was substantially above the market price for a share of Piper stock, the opportunity for stock manipulations and unfair dealings in Piper stock by those who may have learned of the agreement prior to its becoming public knowledge was apparent. The May 8th press release would therefore appear both desirable and consonant with the directives of Securities & Exch. Comm'n v. Texas Gulf Sulphur Co., 401 F.2d 833 (2d Cir. 1968), *cert. denied*, Coates v. Securities & Exch. Comm'n, 394 U.S. 976, 89 S.Ct. 1454, 22 L.Ed.2d 756 (1969). Further,

[3] *Supra* note 1 at 9.

the guidelines for press releases issued by the Exchange on July 19, 1968 support this policy of timely disclosure.

> "Negotiations leading to acquisitions and mergers, stock splits, the making of arrangements preparatory to an exchange, or tender offer, * * * are the type of developments where the risk of untimely and inadvertent disclosure of corporate plans is most likely to occur. Frequently, these matters require discussion and study by corporate officials before final decisions can be made. Accordingly, extreme care must be used in order to keep the information on a confidential basis.
>
> "Where it is possible to confine formal or informal discussions to a small group of the top management of the company or companies involved and their individual confidential advisors where adequate security can be maintained, premature public announcement may properly be avoided. * * *
>
> "At some point it usually becomes necessary to involve other persons to conduct preliminary studies or assist in other preparations for contemplated transactions, e. g., business appraisals, tentative financing arrangements, attitude of large outside holders, availability of major blocks of stock, engineering studies, market analyses and surveys, etc. Experience has shown that maintaining security at this point is virtually impossible. Accordingly, *fairness requires that the Company make an immediate public announcement as soon as confidential disclosures relating to such important matters are made to 'outsiders.'*
>
> "The extent of the disclosures will depend upon the stage of discussion, studies, or negotiations. So far as possible, public statements should be definite as to *price*, ratio, timing and/or any other pertinent information

necessary to permit a reasonable evaluation of the matter. As a minimum, they should include those disclosures made to 'outsiders'." (Emphasis added.) New York Stock Exchange Company Manual at A–19 (July 19, 1968).

Section 5(c) of the Securities Act of 1933 makes it unlawful for any person directly or indirectly, to offer to sell or offer to buy any security unless a registration statement has been filed as to such security. The May 8th press release, however, merely asserts that Bangor Punta has agreed to file a registration statement with the SEC covering a proposed exchange offer for any and all of the remaining outstanding shares of Piper for a package of Bangor Punta securities. On its face, this press release cannot itself be construed as an offer to sell or buy securities. This view is supported by SEC Rule 135, which, in pertinent part, provides:

> "(a) For the purposes only of Section 5 of the Act, the following notices sent by an issuer in accordance with the terms and conditions of this rule shall *not* be deemed to offer any security for sale:
>
> * * * * * *
>
> "(2) A notice to any class of security holders of such issuer or of another issuer advising them that it proposes to offer its securities to them in exchange for other securities presently held by such security holders * * *." (Emphasis added.)

Chris-Craft argues further than in addition to Section 5(c) and Rule 135, Rules 10b–5, 17 C.F.R. § 240.10b–5, and 10b–6, 17 C.F.R. § 240.10b–6, forbid a person making an exchange offer from placing a value on the securities being

offered, since any opinion as to value might be self-serving and misleading.

SEC Rule 135 provides that "(a) notice to any class of security holders * * * advising them that it proposes to offer its securities to them in exchange for other securities presently held by such security holders * * * shall contain * * * the name of the issuer and the title of the securities to be surrendered in exchange for the securities to be offered, [and] the basis upon which the exchange is proposed to be made * * *."

Since, as previously noted, the precise components which were to comprise the package of Bangor Punta securities to be offered for each share of Piper had not been determined at the time of the May 8th press release, Bangor Punta and Piper could do no more than set forth the basis upon which the exchange offer was proposed in the same terms as contained in the May 8th agreement. Additionally, since the Exchange's guidelines for press releases prescribed that "[s]o far as possible, public statements should be definite as to price, ratio, timing and/or any other pertinent information necessary to permit a reasonable evaluation of the matter", the reference to the $80.00 figure cannot be deemed unjustified.

Nor can it be said, as Chris-Craft urges, that Piper and Bangor Punta have, by means of the May 8th press release and the latter's preliminary and final prospectuses, deliberately misled the public into believing that Bangor Punta would, in exchange for each share of Piper, tender securities immediately salable for $80.00, in violation of Sections 9, 10(b) and 14(e) of the Securities Exchange Act of 1934 as amended 15 U.S.C. § 78i, 15 U.S.C. § 78j(b), 15 U.S.C. §78n (e), respectively, and of the rules promulgated with respect to each such Act.

Judge Tenney's Opinion

On July 18, 1969, First Boston rendered a formal opinion to Bangor Punta and Piper that based on the market and other conditions existing prior to the opening of business on July 18, 1969, the combination of securities provided for in the general exchange offer outlined in the registration statement had a value of not less than $80.00.

Such a determination, of course, is normally not a mechanical task but is essentially a matter of judgment. This evaluation was arrived at by a committee of eleven experienced and knowledgeable personnel. In reaching its collective judgment, the committee met on two different occasions to consider all the facts they deemed relevant. Additionally, over six weeks were spent in preparing the material upon which the committee relied.[4] No persuasive argument has been presented to the effect that the value placed on the package of Bangor Punta securities by First Boston was not reached in good faith. Surely, there is no basis for implying from the May 8th press release that such value would endure for the duration of the exchange offer, or be immediately realizable on any particular day. The vagaries of the marketplace belie such a construction. The value placed on the package may vary from buyer to buyer and from day to day. With this in mind, Bangor Punta specified at two places in its final prospectus, at the insistence of the SEC, that:

> "No guarantee of, or representation as to, the value of the securities offered by Bangor Punta pursuant to the Exchange Offer is or can be made."

"Clear misleading statements need be shown * * * before this court can enjoin a tender offer. * * * In the instant case the plaintiffs have failed to show clear mislead-

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[4] Affidavit of John S. Buckley, dated August 4, 1969, at 2.

ing representations in the tender offer or the absence of statements in the tender offer which in combination with other representations would lead to a conclusion that fraud was being perpetrated upon unsuspecting shareholders." Jacobsen Mfg. Co. v. Sterling Precision Corp., 282 F.Supp. 598, 603 (E.D.Wis.1968); Fleischer and Mundheim, Corporate Acquisition by Tender Offer, 115 Penn.L.Rev. 317, 338 (1967).

[2] Chris-Craft's contention that the letters of June 4 and June 20, 1969, sent to all Piper shareholders by W. T. Piper, Jr., Chairman of the Board of Directors and President of Piper, urging acceptance of the Bangor Punta exchange offer, violated Section 14(e) of the Securities Exchange Act of 1934, as amended, 15 U.S.C. § 78n(e), in failing to disclose that the Piper family might obtain additional securities if Bangor Punta was successful in gaining control of Piper, is unsound. This adjustment, provided for in the agreement of May 8th, was designed to compensate the Piper family for having fixed its exchange package more than two months prior to the effective date of the exchange offer and at a lower value than the initial package offered to the public. Simply put, it merely provided protection for the Piper family should the market value of the securities they were to receive be less than the value of the securities offered to other Piper shareholders. Realistically, I cannot say that there is a substantial likelihood that but for this omission in the letters of June 4 and June 20, 1969, a Piper shareholder would have accepted the Chris-Craft exchange offer rather than the Bangor Punta exchange offer. See General Time Corp. v. Talley Indus., Inc., 403 F.2d 159, 162 (2d Cir. 1968), *cert. denied*, 393 U.S. 1026, 89 S.Ct. 631, 21 L.Ed.2d 570 (1969).

A copy of the agreement of May 8th, which contained this provision, was filed with the SEC on May 29, 1969, as **(7122 App. A)**

an exhibit to the registration statement. Further, James J. Rochlis and C. Leonard Gordon, officers and directors of Chris-Craft, explained this provision in detail in a letter sent to all Piper shareholders prior to the issuance of Bangor Punta's final prospectus. At the suggestion of the SEC, reference to the possibility that the Piper family's package might be increased in the event Bangor Punta obtained control of Piper was printed on the cover page of Bangor Punta's final prospectus.[5] "Surely stockholders, once informed of the facts, have a right to make their own decisions in matters pertaining to their economic self-interest, whether consonant with or contrary to the advice of others, whether such advice is tendered by management or outsiders or those motivated by self-interest." American Crystal Sugar Co. v. Cuban-American Sugar Co., 276 F.Supp. 45, 50 (S.D.N.Y.1967).

[3] Rule 10b-6, 17 C.F.R. § 240.10b-6, provides that it shall constitute a "manipulative or deceptive device or contrivance" under Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b), for an underwriter to purchase securities while he is still participating in their distribution.[6] R. A. Holman & Co. v. Securities & Exch. Comm'n, 366 F.2d 446 (2d Cir. 1966), *opinion amended on rehearing*, 377 F.2d 665 (2d Cir.), *cert. denied*, 389 U.S. 991, 88 S.Ct. 473, 19 L.Ed.2d 482 (1967), *rehearing denied*, 389 U.S. 1060, 88 S.Ct. 767, 19 L.Ed.2d 867 (1968). Manipulation was one of the basic evils with which Congress was concerned in enacting statutes to regulate the securities market. See

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[5] Affidavit of John J. Martin, dated August 4, 1969, at 4-5.

[6] "Distribution" comprises "the entire process by which in the course of a public offering the block of securities is dispersed and ultimately comes to rest in the hands of the investing public." Lewisohn Copper Corp., 38 S.E.C. 226, 234 (1958).

Section 2(3) of the Securities Exchange Act of 1934, 15 U.S.C. § 78b(3). Manipulation was often accomplished by those about to sell securities or already engaged in selling them, bidding on the market for the same securities, thereby creating an unjustifiable impression of market activity which would facilitate the sale at artificially high prices. As was noted in Securities & Exch. Comm'n v. Scott Taylor & Co., 183 F.Supp. 904, 907 (S.D.N.Y.1959): "This was one of the practices which the Securities Exchange Act was designed to eradicate, and it is *the* practice which is covered by Rule X-10B-6." (Footnotes omitted.) (Emphasis added.) Weitzen v. Kearns, 271 F.Supp. 616, 623 (S.D.N.Y.1967); Securities & Exch. Comm'n v. Electronics Security Corp., 217 F.Supp. 831, 836 (D.Minn.1963). Bangor Punta's cash purchases of 120,200 shares of Piper in five transactions in May 1969, effected neither on the Exchange nor from or through a broker or dealer, were obviously not designed to place market pressures on the distribution price of Piper, so as to create an artificially high price for this security. Any increase in the price of Piper shares as a result of these transactions would obviously serve only to make Bangor Punta's exchange offer appear less desirable to Piper shareholders.

The SEC has recently proposed Rule 10b-13, which would prohibit a person making a cash tender or exchange offer for any equity security from purchasing such securities otherwise than pursuant to the cash tender or exchange offer. Although the release states that this new Rule is, in effect, a codification of existing interpretations under Rule 10b-6,[7] this Court has been unable to find, and has not been referred to, any support therefor. Moreover, the recent decision in Armour & Co. v. General Host Corp., 296

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[7] Release No. 34—8595, May 5, 1969, CCH § 77,706.

F.Supp. 470, 476 (S.D.N.Y.1969), would appear to the contrary.

> "[S]ubstantial legal issues exist whether Rule 10-b(6) is applicable at all to the instant transactions. The principal question is whether subsection (b) of the Rule applies to the stock of the 'target' corporation [Piper], as well as that of the distributor."

Finally, in considering Chris-Craft's contentions that Bangor Punta and Piper have violated the terms of the final judgment of permanent injunction in making various statements which have been attributed to them by the press, it is well to remember that such episodes may reflect "the difficulties commonly experienced in answering skilled and energetic reporters who seek more definiteness than there is, and the frailties inevitable in human communication * * *." Electronic Specialty Co. v. International Controls Corp., 409 F.2d 937, 951 (2d Cir. 1969). This, of course, would appear especially true when both Piper and Bangor Punta have expressly denied ever making such statements.[8]

It has been frequently noted that a preliminary injunction is an extraordinary equitable remedy which will be granted only upon a showing by the applicant therefor that it will probably succeed on the trial and that it will suffer irreparable injury if the defendant is not restrained from certain activity pending trial. American Metropolitan Enterprises of N. Y., Inc. v. Warner Bros. Records, 389 F.2d 903 (2d Cir. 1968), and the cases cited therein; Clairol Inc. v. Gillette Co., 389 F.2d 264 (2d Cir. 1968) (preliminary injunction will not be granted except upon a clear showing of probable success).

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[8] Affidavit of Donald L. Deming, dated August 4, 1969, at 16; *supra* note 1 at 14-15.

[4] As previously noted, both the Chris-Craft and Bangor Punta exchange offers have expired. Neither party has gained control of Piper, and both are still in a position to do so. Although a finding by the trial court that plaintiff will ultimately prevail on the merits is not required before issuing a preliminary injunction when, as here, there would appear to be a lack of an adequate showing of irreparable damage, the party seeking a preliminary injunction has the burden of convincing the trial court with reasonable certainty that it will succeed upon the trial. Unicon Management Corp. v. Koppers Co., Inc., 366 F.2d 199, 204-05 (2d Cir. 1966). To show irreparable injury, Chris-Craft must at least demonstrate that "unless an injunction is granted, the plaintiff will suffer harm which cannot be repaired." Studebaker Corp. v. Gittlin, 360 F.2d 692, 698 (2d Cir. 1966). No such showing has been made herein; nor does it appear that the "balance of hardships" tip decidedly toward plaintiff.

[5] "The historic injunctive process was designed to deter, not to punish." Hecht Co. v. Bowles, 321 U.S. 321, 329-30, 64 S.Ct. 587, 592, 88 L.Ed. 754 (1944); Hambros Bank, Ltd. v. Meserole, 287 F.Supp. 69, 72 (S.D.N.Y.1968). The conduct of Bangor Punta must be tested, as the Court of Appeals for the Second Circuit noted in both Electronic Specialty Co. v. International Controls Corp., *supra* at 948 of 409 F.2d, and Symington Wayne Corp. v. Dresser Industries, Inc., 383 F.2d 840, 843 (2d Cir. 1967), by whether " 'any of the stockholders who tendered their shares would probably not have tendered their shares if the alleged violations had not occurred.' " After careful consideration, I cannot say that in the instant suit such would have been the case. The equities of the situation would, therefore, appear to speak against the issuance of a preliminary injunction. Armour & Co. v. General Host Corp., *supra* at 475 of 296 F.Supp.

It is not unlikely that further exchange offers to the remaining public shareholders of Piper may now be contemplated both by Bangor Punta and Chris-Craft. In this respect, then, it is wise to recall, as was noted in Sherman v. Posner, 266 F.Supp. 871, 874 (S.D.N.Y. 1966), that:

> "[N]o matter how clearly it was indicated otherwise, the issuance of the injunction undoubtedly would be viewed by some [of these Piper shareholders] as a favorable adjudication of the claims of the plaintiff. This would be tantamount to a determination of wrongdoing on the part of the * * * [Bangor Punta] management. Just how this result could be remedied in the event it was found at a full hearing that the claims of the plaintiff were unfounded is not readily perceptible to this court."

See Kauder v. United Board & Carton Corp., 199 F.Supp. 420, 424 (S.D.N.Y. 1961); Mack v. Mishkin, 172 F.Supp. 885, 889 (S.D.N.Y. 1959).

Accordingly, and for the foregoing reasons, plaintiff's motion is in all respects denied.

So ordered.

APPENDIX B

Opinion of the Second Circuit Court of Appeals. Sitting *in banc* in *Chris-Craft Industries, Inc.* v. *Bangor Punta Corporation and David W. Wallace*, dated April 28, 1970

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 249—September Term, 1969.

(Submitted to the court *in banc*
February 2, 1970* Decided April 28, 1970.)

Docket No. 33983

CHRIS-CRAFT INDUSTRIES, INC.,

Plaintiff-Appellant,

v.

BANGOR PUNTA CORPORATION and DAVID W. WALLACE,

Defendants-Appellees.

Before:

LUMBARD, *Chief Judge,*
WATERMAN, MOORE, FRIENDLY,** SMITH, KAUFMAN,
HAYS, ANDERSON and FEINBERG, *Circuit Judges.*

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* Argued on September 19, 1969 before a division of the court composed of Chief Judge Lumbard and Judges Waterman and Kaufman. After the filing of panel opinions on November 6, 1969 a petition for rehearing with suggestion that the full court also rehear the case was timely filed. The division denied the rehearing petition as of January 12, 1970, but a rehearing *in banc* was then granted, the *in banc* reconsideration to be had without further oral argument. The parties were granted permission to file further briefs on or before February 2, 1970.

** After the nine active judges decided to rehear the case *in banc* Judge Friendly refrained from any further participation in the disposition of the case.

April 28, 1970, Second Circuit Opinion

Appeal from an order denying a motion for an injunction *pendente lite*, United States District Court for the Southern District of New York, Tenney, *J.* Order affirmed. However, as the rationale of affirming opinion differs materially from rationale of opinion below the case is remanded for further proceedings.

ARTHUR L. LIMAN, JOSEPH J. ACKELL, ALAN L. SCHLOSSER, PAUL, WEISS, GOLDBERG, RIFKIND, WHARTON & GARRISON, New York City, *for Plaintiff-Appellant.*

JAMES V. RYAN, WILLIAM L. D. BARRETT, NANCY L. PASLEY, WEBSTER, SHEFFIELD, FLEISCHMANN, HITCHCOCK & BROOKFIELD, New York City, *for Defendants-Appellees.*

PAUL G. PENNOYER, JR., ZACHARY SHIMER, IRENE CONRAD WARSHAUER, CHADBOURNE, PARKE, WHITESIDE & WOLFF, New York City, *for Piper Aircraft et al.*

PHILIP A. LOOMIS, JR., General Counsel; David Ferber, Solicitor; Meyer Eisenberg, Associate General Counsel; Harvey A. Rowen, Attorney, Securities & Exchange Commission, *for Amicus Curiae.*

WATERMAN, *Circuit Judge*:

Plaintiff-appellant, Chris-Craft Industries, Inc., appeals from the denial of an order entered below in the United States District Court for the Southern District of New York denying appellant's motion for a preliminary injunction to

restrain Bangor Punta Corporation from gaining and exercising control of Piper Aircraft Corporation pending a trial on the merits of whether certain shares of Piper were acquired by Bangor Punta in violation of governing Rules of the Securities and Exchange Commission. We affirm the denial of the preliminary injunction but remand the case to the district court for further proceedings there not inconsistent with the within opinion.

This litigation comes at the end of a hard fought battle between Chris-Craft Industries and Bangor Punta Corporation for control of Piper Aircraft Corporation. The contest opened in January 1969 when Chris-Craft began to acquire Piper shares on the open market. At that time Piper had 5,000,000 authorized shares of $1.00 par common stock of which 1,641,890 shares were issued and outstanding. In January 1969 Chris-Craft made a public exchange offer for 300,000 Piper shares, and by February these efforts had gained Chris-Craft 34 per cent of the then outstanding Piper stock. On February 27, 1969, Chris-Craft filed with the Securities and Exchange Commission a registration statement and proposed prospectus for an exchange offer for an additional 300,000 shares. Still another exchange offer was announced by Chris-Craft on May 7 and became effective July 24.

Chris-Craft's bid for control met strong resistance from the Piper family and Piper management, who owned 501,090 shares (31 per cent of the outstanding shares), and considered Chris-Craft to be a corporate raider. The management advised other Piper shareholders that Chris-Craft's tender offer was inadequate but offered 300,000 of Piper's authorized but unissued shares to Grumman Aircraft Corporation at the same price that Chris-Craft had offered. Although this transaction was never consummated, Piper initially advertised that Grumman had agreed to purchase

the Piper shares and the court below noted that Chris-Craft's tender offer was adversely affected by this publicity.

Subsequently, on March 22, the Piper management issued 469,199 shares of authorized but unissued stock to acquire control of two subsidiary corporations, United States Concrete Pipe Company of Florida and Southply, Inc. Piper failed to seek the approval of the New York Stock Exchange and of its own shareholders as its listing agreeement with the Exchange provided it should before issuing a significant new block of stock. Therefore, the Exchange refused to approve Piper's listing application. When the Exchange shortly afterward suspended trading in Piper shares and authorized proceedings before the SEC to delist Piper, Piper rescinded both transactions and trading in its shares was resumed.

At this juncture, in April 1969, the Piper family resumed talks which had begun as early as January with Bangor Punta Corporation. These negotiations bore fruit on May 8, when the two groups agreed that the family would exchange its 501,090 shares for specified Bangor Punta securities. Bangor Punta agreed in addition to use its best efforts to acquire enough additional Piper shares to make it the holder of more than 50% of the shares outstanding. As part of these best efforts, Bangor Punta agreed to make an exchange offer to all Piper shareholders "under which such holders will be entitled to exchange each share of Piper common stock held by them for Bangor Punta securities and/or cash having a value, in the written opinion of The First Boston Corporation, of $80 or more." If Bangor Punta succeeded in acquiring 50% or more of the stock, the consideration paid by Bangor Punta would be increased to make up to the Piper family the difference, if any difference there were, between the value of the package specified in the agreement and $80 per share.

The two occurrences which form the basis of Chris-Craft's complaint followed the negotiation of this contract. The first of these occurrences was the issuance by Bangor Punta and the Piper management of press releases announcing the transaction on May 8, the day the contract was signed and the day after Chris-Craft announced the terms of its second exchange offer. After stating that the Piper family would receive Bangor Punta securities for their shares, the Bangor Punta press release continued as follows:

> Bangor Punta has agreed to file a registration statement with the SEC covering a proposed exchange offer for any and all of the remaining outstanding shares of Piper Aircraft for a package of Bangor Punta securities to be valued in the judgment of The First Boston Corporation at not less than $80 per Piper share. The registration statement covering all securities to be issued will be filed as soon as possible and a meeting of the shareholders of Bangor Punta Corporation will be called for approval.
>
> Mr. Piper said that in view of Bangor Punta's long-standing policy of maintaining autonomy in the management of its operating companies, and the similarity of operating philosophies between the two companies, he and the Piper family would strongly support the merger and would recommend it to all shareholders.
>
> Mr. Wallace said Bangor Punta welcomed the association with Piper Aircraft, its world-wide distribution, and its prestigious product name. He said the consolidation would align the Piper Aircraft name with other leading Bangor Punta companies, including Smith & Wesson, Starcraft Company, and Waukesha Motor Company.

> Bangor Punta manufactures a wide variety of recreational vehicles including sailboats, houseboats, snowmobiles, campers, trailers and motor homes. A merger of Bangor Punta and Piper Aircraft would bring Bangor Punta into the light aircraft manufacturing business.
>
> Sales of the combined companies would reach $450,000,000 in fiscal 1969, with approximately $180,000,000, or 40%, in the aircraft, recreational and leisure time fields.

Piper Aircraft Corporation simultaneously issued a similar press release.

These announcements attracted an immediate response from the Securities and Exchange Commission, which felt that the release constituted an offer to sell securities before any registration statement had been filed. Accordingly the SEC instituted an action against Bangor Punta and Piper in the United States District Court for the District of Columbia on May 26, and on the same day the defendants consented to the entry of judgment and the issuance of an injunction prohibiting further releases of a similar nature before Bangor Punta's registration statement and prospectus were filed.

The second occurrence or set of occurrences of which Chris-Craft complains took place between May 14 and May 23, when Bangor Punta purchased 120,200 shares of Piper stock for cash in private transactions. Chris-Craft alleges that on April 7, 1969, the staff of the SEC warned Chris-Craft's top executives that continued cash purchases of Piper stock while Chris-Craft's own exchange offer was outstanding, as the first one then was, would be regarded by the SEC as a violation of Rule 10b-6, which prohibits

an issuer from purchasing securities while still participating in their distribution. Chris-Craft did refrain from further purchases during the remainder of its first tender offer and all of its second. Bangor Punta's purchases of stock between May 14 and May 23 occurred while its exchange offer was outstanding if one assumes that the May 8 press release constituted an offer to sell, as the SEC charged that it did. Bangor Punta states that although the SEC knew of its cash purchases at the time the consent decree was discussed, May 23 to May 26, the SEC nonetheless failed to challenge these purchases or ask for their rescission. However, it is undisputed that the SEC announced publicly its position on such purchases in a press release issued May 5.

Bangor Punta's exchange offer closed on July 29, and Chris-Craft's second offer ended August 4. At that time Bangor Punta held 45% of Piper's stock, and Chris-Craft held 40%. By the time this case came to argument on appeal, Chris-Craft had increased its holdings to 46.2% of Piper's common stock, while Bangor Punta had finally acquired a majority with 52.7%.

Chris-Craft commenced the present lawsuit on July 22, 1969, seeking a preliminary injunction which would order Bangor Punta (1) to offer the right to rescind to all persons who had tendered Piper shares to Bangor Punta pursuant to its exchange offer, (2) to refrain from acquiring further Piper shares, (3) to refrain from effecting a merger of Piper and Bangor Punta, and (4) to refrain from voting the 120,200 Piper shares acquired for cash between May 16 and May 23, 1969. The district court denied Chris-Craft's motion for a preliminary injunction, citing both the lack of any irreparable injury to Chris-Craft if the motion were denied and the lack of any illegal behavior

on the part of Bangor Punta. Chris-Craft then sought and received an expedited appeal to this court.

The Preliminary Injunction

We agree with the district court that a preliminary injunction is not warranted. A preliminary injunction should issue only when it is needed "as an equitable policing measure to prevent the parties from harming one another during the litigation," *Hamilton Watch Co.* v. *Benrus Watch Co.*, 206 F.2d 738, 742 (2 Cir. 1953). It is apparent that here there is no threat that unless an injunction issues before trial "the plaintiff will suffer harm that cannot be repaired." *Studebaker Corp.* v *Gittlin*, 360 F.2d 692, 698 (2 Cir. 1966). Counsel for Bangor Punta has orally stipulated at argument that no merger between that company and Piper will be effected before the end of this litigation, so that no injunction restraining a merger is needed. We do not see, and Chris-Craft does not suggest, what other irreparable harm might result from Bangor Punta's voting the 120,200 shares acquired for cash in May.

Absent any such prejudice from the voting of the stock we do not see how harm to plaintiff can result from refusing to order before the merits of the case are adjudicated after a trial a divestiture or rescission of stock acquired by Bangor Punta during its exchange offer. Indeed, to "give to a plaintiff all the actual advantage which could be obtained by the Plaintiff as a result of a final adjudication of the controversy in favor of the plaintiff" would be clearly inequitable under such circumstances. *Selchow & Richter Co.* v. *Western Printing & Lith. Co.*, 112 F.2d 430, 431 (7 Cir. 1940). We also understand counsel for Chris-Craft to admit on oral argument that because of its complexity an order for rescission or divestiture should be worked out only at trial.

Finally, we conclude that the district court did not err in refusing to enjoin the continued solicitation of stock by Bangor Punta. At that time Chris-Craft was free to compete equally with Bangor Punta for the remaining Piper shares, and it did so. We do not understand Chris-Craft to allege that prior misdeeds of Bangor Punta so determined the course of the competition for shares after the date of the decision below that Chris-Craft was placed at any real disadvantage. Consequently, we affirm the denial of the preliminary injunction.

However, we also feel compelled to pass on the district court's alternative holding that Bangor Punta did not violate the securities laws, for it is clear that this ruling below would determine the outcome of the trial on the merits. On this issue we disagree with the district court.

The May 8 Press Releases

Section 5(c) of the Securities Exchange Act of 1933, as amended, states in part that:

> (c) It shall be unlawful for any person, directly or indirectly, to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to offer to sell or offer to buy through the use or medium of any prospectus or otherwise any security, unless a registration statement has been filed as to such security . . . .

Section 5(b) of the Act provides that offers to sell may be made after the registration statement is filed, but before it becomes effective, provided the offers are made by specified means which include the use of a prospectus meeting the requirements of Section 10.

The Securities and Exchange Commission has promulgated Rule 135 to exempt certain disclosures of forthcoming

issuances from the definition of an "offer to sell" prohibited by Section 5(c). This Rule reads in relevant part as follows:

> (a) For the purposes only of section 5 of the Act, the following notices sent by an issuer in accordance with the terms and conditions of this rule shall not be deemed to offer any security for sale:
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> * * * * *
>
> (2) A notice to any class of security holders of such issuer or of another issuer advising them that it proposes to offer its securities to them in exchange for other securities presently held by such security holders;
>
> * * * * *
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> (b) Such notice shall be sent not more than 60 days prior to the proposed record date for determining the security holders entitled to subscribe to the securities or, if there is no such record date, not more than 60 days prior to the proposed date of the initial offering of the securities.
>
> (c) The notice shall state that the offering will be made only by means of a prospectus which will be furnished to such security holders or employees, as the case may be, and shall contain no more than the following additional information:
>
> (1) The name of the issuer;
>
> (2) The title of the securities proposed to be offered;
>
> * * * * *
>
> (4) In the case of an exchange offering, the name of the issuer and the title of the securities to be sur-

rendered in exchange for the securities to be offered, the basis upon which the exchange is proposed to be made and the period during which the exchange may be made, or any of the foregoing;

* * * * *

(6) Any statement or legend required by State law or administrative authority.

Chris-Craft argues, and the argument is supported by the SEC, both in its action filed May 26 against Bangor Punta and in its *amicus curiae* brief in this court, that the categories of information privileged under the Rule are exclusive. In view of this exclusivity they contend that as the rule does not mention disclosure of the value of the securities to be offered, Bangor Punta's and Piper's announcements that the package of securities offered by Bangor Punta would be valued at $80 oversteps the exemption and makes the press release an offer to sell.

We agree with this contention. When it is announced that securities will be sold at some date in the future and, in addition, an attractive description of these securities and of the issuer is furnished, it seems clear that such an announcement provides much the same kind of information as that contained in a pospectus. See *SEC* v. *Arvida Corp.*, 169 F. Supp. 211 (SDNY 1958). Doubtless the line drawn between an announcement containing sufficient information to constitute an offer and one which does not must be to some extent arbitrary. A checklist of features that may be included in an announcement which does not also constitute an offer to sell serves to guide the financial community and the courts far better than any judicially formulated "rule of reason" as to what is or is not an offer. Rule 135 provides just such a checklist, and if the Rule is not construed

as setting forth an exclusive list, then much of its value as a guide is lost.

Moreover, it is reasonable to conclude that the assigning of a value to offered shares constitutes an offer to sell. One of the evils of a premature offer is its tendency to encourage the formation by the offeree of an opinion of the value of the securities before a registration statement and prospectus are filed. There is then no information on file at the SEC by which the Commission can check the accuracy of the information which forms the basis of the offeror's estimate of value, and any offeree, such as the reader of a press release, is encouraged to form a premature opinion of value without benefit of the full set of facts contained in a prospectus.

Here a statement of the value of the securities Bangor Punta offered was made directly in the announcement. It is true that the value which the reader of the May 8 press releases could be expected to accept is a value based upon the opinion of a reputable financial corporation and not upon general and necessarily speculative facts about the nature of the offeror's business, as in *Arvida, supra.* However, the true significance of the $80 value which Bangor Punta claimed for its securities package was nonetheless unclear. Chris-Craft charges that the figure constituted an outright misrepresentation inasmuch as most readers would construe the figure as representing the market value of the package. In fact, Chris-Craft charges, some of the securities in the package had not previously been sold on the market at all, and the market value of Piper shares never reached $80 in response to the Bangor Punta exchange offer, so that the Bangor Punta securities did not have an $80 market value and could not honestly have been thought to have such a value. We need not reach the question whether prudent investors would have so construed the $80

value or whether it would have been assumed, as was apparently the case, that the value referred to was based on such considerations as Bangor Punta's earnings and asset value as well as upon the sales price of the securities. It is enough to point out that under either construction the SEC had no way of checking the honesty of the figure, and that the public did not receive the detailed information it would have received from a prospectus issued after a registration statement had been filed. Such information would have eliminated the possibility, perhaps the probability, that some persons would have construed the $80 figure as referring to market value when that value was neither accurate nor intended.[1]

Bangor Punta and Piper argue that even prior to the filing of a registration statement an immediate disclosure of market value is compelled in cases such as this both by *SEC* v. *Texas Gulf Sulphur Co.*, 401 F.2d 833 (2 Cir. 1968), *cert. denied as to issues not pertinent here*, sub nom. *Coates* v. *SEC*, *Kline* v. *SEC*, 394 U.S. 976 (1969), and by the rules of the New York Stock Exchange. We do not agree. The only material fact in this case within the meaning of *Texas Gulf Sulphur* was Bangor Punta's commitment to offer its securities for Piper Aircraft shares. Rule 135 provides adequately for the announcement of a material fact such as this; further disclosure would, as stated above, thwart other policies of the securities laws. Had Bangor Punta observed Rule 135 by revealing immediately its intention to make an exchange offer and by later revealing the titles of the securities it proposed to offer and the basis or ratio on which the exchange was proposed to be made as soon as

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[1] The prospectus which Bangor Punta later issued contained a complete description of the securities it was offering for Piper stock, including the over-the-counter sales price of those securities to which such a price was applicable.

these matters were decided, adequate information concerning the proposed transaction would have been placed before the public and the potentially misleading estimate of value would have been avoided.[2] Even if we assume that knowledge of the value figure involved here might conceivably have conferred some benefit on insiders had it not been revealed, we feel that this risk of unfair advantage is outweighed by the danger that substantial numbers of investors were misled by the figure's publication. The fact that a few additional sophisticated investors could have discovered the $80 value guarantee in the description of the transaction which Bangor Punta filed with the SEC pursuant to Section 13(d) of the 1934 Act is of no moment. Such investors would almost certainly be small in number, and any arguable danger of permitting them an unfair advantage is outweighed by the stronger probability that the press release misled a large number of unsophisticated investors.

The same principles apply to the New York Stock Exchange's requirement[3] that insiders disclose information likely to affect the market unless such information can be restricted to a small group of top management officials. In any event, a policy of the New York Stock Exchange, although entitled to considerable respect, cannot bind the Commission or the courts. *Silver* v. *New York Stock Exchange*, 373 U.S. 341, 357 (1963). To hold that disclosure would be privileged here because the $80 value could not be kept secret and might affect the market would mean that many other companies could offer to sell securities before their registration by claiming that the terms of the proposed offer could not be kept totally secret and must

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[2] See, generally, SEC Release No. 33-5009 (Oct. 7, 1969).

[3] New York Stock Exchange Co. Manual, Section A2.

therefore be disclosed in full. Consequently we hold that the May 8 press release by Bangor Punta violated Section 5(c) and therefore we remand the action to the district court for it to consider in light of this opinion and with the benefit of any further evidence which the parties may present at trial what the most suitable remedy for the violation might be.

Bangor Punta's Purchases of Stock During Its Exchange Offer

Rule 10b-6 forbids "any person . . . (2) who is the issuer or other person on whose behalf . . . a distribution is being made . . . to bid for or purchase for any account in which he has a beneficial interest, any security which is the subject of such distribution . . . or any right to purchase any such security . . . ."

On May 5, 1969, before the purchases of which Chris-Craft complains, the SEC issued release No. 34-8595, announcing a proposed Rule 10b-13. This Rule, which did not become effective until November 10, 1969, reads in part as follows:

> (a) No person who makes a cash tender offer or exchange offer for any equity security shall, directly or indirectly, purchase, or make any arrangement to purchase, any such security (or any other security which is immediately convertible into or exchangeable for such security), otherwise than pursuant to such tender offer or exchange offer, from the time such tender offer or exchange offer is publicly announced or otherwise made known by such person to holders of the security to be acquired until the expiration of the period, including any extensions thereof, during which securities tendered pursuant to such tender offer or

> exchange offer may by the terms of such offer be accepted or rejected; . . . .

The SEC announced in the same release that Rule 10b-13 served only to restate law which already existed:

> This provision is, in effect, a codification of existing interpretations under Rule 10b-6, which among other things, prohibits the person making a distribution from bidding for or purchasing the security being distributed or any right to acquire that security. These interpretations have pointed out that the security to be acquired in the exchange offer is, in substance, either a right to acquire the security being distributed or is brought within the rule under paragraph b thereof; and Rule 10b-6 prohibits the purchase of such security during the distribution except through the exchange offer, unless an exemption is available.

Despite the reference in the Release to "a codification of existing interpretations under Rule 10b-6," neither the SEC nor the parties to this action have cited any such precedents, nor have we found any. However, we do not find this lack of precedent crucial if Rule 10b-6 should independently be found to apply to purchases of stock while exchange offers for such stock are outstanding.

One of the primary purposes of Rule 10b-6 is to prevent an issuer of stock from manipulating the market for that stock. As the court stated in *SEC* v. *Scott Taylor & Co.*, 183 F. Supp. 904, 907 (SDNY 1959):

> Manipulation was often accomplished by those about to sell securities or already engaged in selling securities bidding on the market for the same securities, thereby

> creating an unjustifiable impression of market activity which would facilitate the sale at artificially high prices. This was one of the practices which the Securities Exchange Act was designed to eradicate, and it is the practice which is covered by Rule X-10b-6. (Footnote omitted.)

See also, *Weitzen* v. *Kearns*, 271 F. Supp. 616, 623 (SDNY 1967), *Miller* v. *Steinbach*, 268 F. Supp. 255, 280 (SDNY 1967); *SEC* v. *Electronics Security Corp.*, 217 F. Supp. 831, 836 (D. Minn. 1963).

Bangor Punta argues that its purchase of Piper stock could only serve to drive up the price of Piper stock and thus to make the Bangor Punta shares offered in exchange appear less attractive—the opposite effect from that which Rule 10b-6 would normally seek to prevent. However, this argument overlooks the decided benefits that purchases of target company stock can produce for the initiator of an exchange offer. If the price of the target company's stock does increase in response to cash purchases by the exchange offer or after the offer has been announced, many shareholders in the target company are likely to assume that the price increase results solely from the bullish effect of the exchange offer on the market. Small investors especially would be likely to assume that the exchange offer was receiving serious attention and approbation from larger, more knowledgeable investors than they. The managements of either the target company or the offeror can compound this impression by announcing the number of shares of target stock acquired by the offeror since the initiation of the exchange offer. Absent some indication to the contrary, the target company shareholders would be likely to assume that the entire increase resulted from the offer, not from cash purchases in addition to the offer.

Prevention of this kind of manipulation seems well within the spirit of Rule 10b-6. It is within the letter of the Rule as well. As quoted above, part (a) of Rule 10b-6 prohibits the issuer of a security not only from purchasing the issued security itself while offering it, but also from purchasing "any right to purchase any such security." Here the Piper shares carried the right to acquire Bangor Punta securities as a result of Bangor Punta's exchange offer. Consequently, we hold that Bangor Punta could not lawfully purchase these shares during the tenure of its exchange offer.

It remains open to Bangor Punta to demonstrate at trial that its purchases fall within the exemption provided by Rule 10b-6 for "unsolicited . . . purchases . . . effected neither on a securities exchange nor from or through a broker or dealer . . . ." Moreover, we do not pass any judgment at this time on the question of what remedy is appropriate in regard to Bangor Punta's unlawful purchases of stock, nor on the significance of the fact that Chris-Craft itself purchased stock during an exchange offer prior to the SEC's warning.

We remand for further proceedings not inconsistent with this opinion.

MOORE, *Circuit Judge* (concurring in part):

I concur in the affirmance of the order denying a preliminary injunction. Under customery procedure, the issues framed by the pleadings would come on for trial. Upon such facts as might be developed upon such a trial and the conclusions of law found to be applicable thereto, the case would come before us on appeal. In this case, however, the majority, in effect, give their conclusions of law before trial and appeal.

Quite apart from giving the trial court an opportunity to fulfill its role in arriving at a decision, the majority, in their advisory opinion, misconstrue, I believe, the May 8th press release and Rule 135.

There should be little doubt that if the May 8th agreement had been misstated, a suit, alleging misrepresentation and fraud, would be before us. And yet any omission of the all important terms proposed would have been materially misleading. The exchange was to be for "Bangor Punta securities and/or cash having a value, in the written opinion of The First Boston Corporation, of $80 or more." This was "the basis upon which the exchange is proposed to be made," Rule 135(c)(4). The "offer to sell" exemption required this information. The most important element of "basis" was, of necessity, some indication as to value. $80 in cash needed no evaluation; the package of securities, not then final, had to have some equivalent measure. To say, as does the majority, that the "announcements that the package of securities offered by Bangor Punta would be valued at $80 oversteps the exemption and, therefore, makes the press release an offer to sell," turn a preliminary and informative press release, which advises the public of a forthcoming registration statement, into a prospectus would—or at least should—come as a shock to the S.E.C.

As to the stock purchases by Bangor Punta during its exchange offer, the age-old question is again presented: does a rule or statute merely codify an existing decision-made rule of law or does it create a new rule? The very fact that Rule 10b-6 was to be quite prospective in operation is rather convincing that the latter is the proper conclusion.

In summary, I would affirm on the only issue before us, the denial of a preliminary injunction, and would withhold

any other opinions until we have an opportunity to pass upon such future appeal as may come before us in this case.

ANDERSON, *Circuit Judge* (concurring):

I concur in the affirmance of the order of the District Court, and in Judge Waterman's discussion of Rule 10b-6. I also concur in the holding that on May 8, 1969, the appellees were neither required nor permitted to disclose more than the fact of Bangor Punta's commitment to make an exchange offer of its securities to the Piper shareholders as part of an agreement to purchase the holdings of the Piper insiders, since the titles of Bangor Punta securities and the basis or ratio of this exchange were not yet established. For the reasons there expressed, the policies of regulation common to the federal securities laws require this resolution of the conflict between openness and reticence in disclosing specific details which is implicit in the dictates of the Securities Exchange Act of 1934 and the Securities Act of 1933.

I would not concur, however, in any interpretation of the opinion which might be thought to suggest that disclosure of information relating to the $80 valuation estimate, specified in the insiders' sale agreement, would not be required under any circumstances because it would fail to satisfy the 1934 Act's standard of materiality, regardless of whether supervening restrictions of the 1933 Act are applicable. As Chief Judge Lumbard's dissent notes, the additional fact that Bangor Punta had committed itself to offer securities valued by a well-known investment banking firm at not less than $80 per Piper share, and to back this commitment with a conditional guarantee of the value of the securities already offered to the Piper insiders, might fall within the investor-oriented definition of materi-

ality set out in relation to disclosure required by §10(b) of the 1934 Act and Rule 10b-5 in *SEC* v. *Texas Gulf Sulphur Co.*, 401 F.2d 833, 849 (2 Cir. 1968), cert. denied sub nom. *Coates* v. *SEC*, 394 U.S. 976 (1969). The Court's holding, in which I concur, is simply that the possible application of disclosure principles discussed in that case is here "outweighed by the danger that substantial numbers of investors were misled by the figure's publication" in a manner violating Rule 135.

Were it necessary to consider the application of materiality tests to the $80 value term, the fact could not be overlooked that Rule 10b-5 applies to the disclosure of all material "information," 401 F.2d at 848, a category of data which may include some "matters which do not fall tidily into either the 'fact' or 'opinion' class." A. Bromberg, *Securities Laws: Fraud—SEC Rule 10b-5*, §7.4(6)(d), p. 187 (1969). But this case does not turn upon either the validity of the distinction between a material "event" and a mere "prediction or opinion" suggested in SEC Release No. 5009 (Oct. 7, 1969), or upon its application to these facts.

LUMBARD, *Chief Judge* (dissenting):

I dissent.

Although I agree with the majority's conclusion that a preliminary injunction is not warranted in this case, I cannot accept the interpretation given by my colleagues to those provisions of the securities laws invoked against Bangor Punta. In my view Judge Tenney was substantially correct in his rulings below, and his order should be affirmed.

This case turns on two events, the issuance of the May 8 press release and Bangor Punta's purchases of 120,200

shares of Piper stock from May 12 through May 24. I think that Bangor Punta acted properly in both situations. Not only was the May 8 release proper, but the parties could have done no less, for I read recent interpretations of the securities laws as imposing an affirmative obligation to disclose the matters announced in the release. As to the purchases of the 120,200 shares, Bangor Punta did not then know of any rule or interpretation precluding the transactions, and the Commission has at least twice passed up opportunities to enforce its "long-established" interpretation of 10b-6 against Bangor Punta. Although it was aware of the purchases when it was preparing its suit in the District Court for the District of Columbia, the SEC made no mention of them in the pleadings nor sought to enjoin Bangor Punta from further purchase in the consent decree. Later, the Commission approved Bangor Punta's registration statement without requiring any disclosure of alleged violations of 10b-6. For the SEC now to take the position that Rule 10b-6 prohibited the purchases represents a complete reversal of the position it had taken towards Bangor Punta until now.

1. *Section 5(c) and Rule 135*

It was entirely proper for Bangor Punta to enter into the May 8th agreement with the Piper family, as the family had every right to choose between takeover by Chris-Craft, Bangor Punta, or any other group.

Bangor Punta agreed to use its best efforts to acquire more than 50% of the Piper Common Stock. As "a part of such best efforts," it promised to "take all steps necessary to make a further exchange offer to all holders of Piper Stock . . ."; each share was to be exchanged for Bangor Punta securities or cash "having a value, in the written opinion of the First Boston Corporation, of $80

or more . . . ." There was a similar provision to safeguard the Pipers in that they would received consideration worth at least $80. Thus, as they well may have had a right to expect, the other shareholders of Piper were assured substantially equal treatment to that received by the Piper family. See *Perlman* v. *Feldmann*, 219 F.2d 173 (2d Cir. 1955); Andrews, The Stockholder's Right to Equal Opportunity in the Sale of Shares, 78 Harv. L. Rev. 505 (1965).

Bangor Punta and Piper immediately notified the Stock Exchange of this agreement and issued a press release on May 8. I think Judge Tenney was correct in holding that the press release was consonant with the exchange guidelines for announcing material corporation developments and with the mandate of *SEC* v. *Texas Gulf Sulphur*, 401 F.2d 833 (2d Cir. 1968), cert. denied, 394 U.S. 976 (1969).

In *Texas Gulf*, we reiterated our view that the securities laws should advance "the justifiable expectation of the market place that all investors trading on impersonal exchanges have relatively equal access to material information . . . ." 401 F.2d at 848. It seems clear that if this principle is to be honored, the agreement with forty members of the Piper family, in conjunction with the decision to launch a tender offer, was material information requiring disclosure.

The majority intimates that the $80 figure was not a material fact, a suggestion with which I cannot agree. The test for materiality laid down in *Texas Gulf* is whether the fact is one to which "[a] reasonable man would attach importance . . . in determining his choice of actions in the transaction in question." 401 F.2d at 849. On May 8 Chris-Craft was offering $65 for each Piper share in a taxable exchange; no reasonable man holding Piper shares on that date would find "unimportant" the fact that Bangor

planned to offer, in the near future, a considerably more attractive package of securities, with a value of approximately $80.

To me, however, finding the fact material does not in every case compel disclosure, for the need for equal access to information does not automatically override competing policies of the securities laws as embodied in other statutory provisions and well-established regulations. Here, Rule 135 advances the basic principle that the prospectus and registration statement shall be the primary source of information during and before a contemplated offering, and only limited kinds of information can be released prior to filing.

The task of harmonizing regulations based on competing policies should of course be left to the SEC in the first instance. But when, as here, the Commission refuses even to recognize the existence of a conflict, we must strike the balance. Fortunately, our task here is not difficult, for there is language in Rule 135 which when read in the light of *Texas Gulf* authorizes the announcement.

Most of the May 8th announcement—the fact of the offering, the proposed date—was clearly authorized by Rule 135. While the $80 figure may seem more difficult to justify, under the circumstances its announcement was the only course open to Bangor Punta. Responding to the problem of valuation, Rule 135(c)(4) provides for notification of "the basis upon which the exchange is proposed to be made. . . ." Although not free from doubt, in the light of *Texas Gulf* I would read this provision as permitting announcement of the $80 figure.

The need for fair and equal access to information about the terms of a tender offer must be balanced against premature and incomplete disclosure of a securities offering in

contravention of the registration and disclosure requirements underlying the 1933 Act. The conflict is sharply posed when, as here, the merger agreement sets only a value for the exchange package, with the underlying securities left to be determined later. When the securities to be offered are not specified at the time of the announcement, the investing public cannot even begin to make an independent evaluation of the offer[1] and perforce may tend to react significantly but blindly to the unsupported dollar sum. Also, I realize there is a possibility for abuse, with companies employing this manner of agreement in order to gain the advantages of "jumping the gun."

Despite these considerations, it seems to me that here the need for disclosure was paramount. In addition to the forty members of the Piper family and their agents, a large group of persons employed by independent firms, including accountants, escrow agents, banks, and printers, would of necessity work on the Piper agreement and so learn of the news. Not bound as insiders[2] or by the restraints of corporate trust imposed on employees of Piper and Bangor Punta, they would be free to trade upon this information, and with Piper trading at a considerably lower price on May 8, their response is easily foreseen. Even if under some legal or moral duty of restraint, a group this large could not be effectively policed or controlled. Further, the figure would rapidly spread; a dollar sum speeds the rumor

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[1] This situation must be distinguished from an agreement stipulating that the undetermined securities are to have a certain cash value. This can occur when the tendering company promises to offer only widely traded securities in its package; then, the market price of widely traded securities as of the date the exchange becomes effective determines the exchange ratio. There, the public is fully protected, and I can see no arguments against full and immediate disclosure.

[2] The status of "insiders" as to all these people has not yet been established and would raise difficult questions of enforcement.

as it is easily remembered and easily transmitted. Finally, Piper stockholders, thus apprised by the May 8 release of what they might receive if they held their shares rather than tendering to Chris-Craft, clearly benefited from the disclosure.[3] Chris-Craft can hardly complain that it was placed at a disadvantage by reason of Bangor Punta's higher bid and its ability to pay more; thus the law of the market place benefits the stockholders whose shares are sought.

On petition for rehearing, another factor compelling disclosure has been called to our attention. The so-called "tender offer" provision, section 13d-1 of the Securities Act of 1934, required Bangor Punta to file a detailed description of the May 8 agreement with the SEC within ten days, by May 18th. When timely filed, the description in accordance with section 13d-1 disclosed as an essential element of the Agreement that Bangor Punta planned a registered offer to the public shareholders of Piper, the offer to consist

> "of cash and/or securities having a value of at least $80 per share. Such value to be determined by The First Boston Corporation . . . ."

This wording is virtually identical to the May 8 announcement.

The 13d-1 statement was placed in the public files of the Commission, a repository over which, it is not unreasonable to assume, the keener investment houses maintain a close scrutiny. Thus, even if it be assumed that no "leaks" of the sort described above would have occurred, sophisticated investors within a few days would have obtained the $80 figure merely by a careful perusal of public records. The policies behind *Texas Gulf* command that such imper-

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[3] Indeed, if the price had not been announced, a Piper stockholder who tendered his shares to Chris-Craft during the interim might well have grounds for an action against Bangor Punta and Piper.

fect dissemination be corrected by broad disclosure through the public media, and Rule 135 must be read so as to permit such a course of action.

It is one thing to recognize the competing considerations and attempt to find a balanced solution and quite another to state flatly, as does the SEC, that the companies are under no duty to disclose. In its *amicus* brief, the Commission argues that Piper and Bangor Punta had no duty even to announce the fact of the agreement, let alone the price, since neither they nor any of their insiders were going to trade in the shares involved. I find this position wholly unrealistic and hardly designed to protect the other Piper stockholders. Simply put, Bangor Punta and Piper realized they were faced with one of "those situations which are essentially extraordinary in nature and which are reasonably certain to have a substantial effect on the market price of the security if [the extraordinary situation is] disclosed." *SEC* v. *Texas Gulf Sulphur*, 401 F.2d 833, 848. Disclosure was required.

Unlike the SEC, the New York Stock Exchange has tried to chart a course which accommodates the competing considerations. A Stock Exchange Rule adopted on July 18, 1968 in the wake of *Texas Gulf* in part provides:

> Negotiations leading to acquisitions and mergers, stock splits, the making of arrangements preparatory to an exchange or tender offer . . . are the type of developments where the risk of untimely and inadvertent disclosure of corporate plans is most likely to occur. . . .
>
> At some point it usually becomes necessary to involve other persons to conduct preliminary studies or assist in other preparations for contemplated transactions. . . . Experience has shown that maintaining security at this point is virtually impossible. Accord-

> ingly, fairness requires that the Company make an immediate public announcement as soon as confidential disclosures relating to such important matters are made to "outsiders."
>
> The extent of the disclosures will depend upon the state of discussion, studies, or negotiations. So far as possible, public statements should be definite as to price, ratio, timing and/or any other pertinent information necessary to permit a reasonable evaluation of the matter. As a minimum, they should include those disclosures made to "outsiders" . . . .

NYSE Company Manual A-19 (July 18, 1969) (Addendum at 19-20). This standard seems to me a realistic solution to the problem.

I would hold that the May 8 announcement was proper, reflecting a fair accommodation of Section 5(c) and Rule 135 and the obligation to disclose material facts.

2. *Rule 10b-6*

Nor would I find that any violation of Rule 10b-6 was occasioned by Bangor Punta's purchases of 120,200 shares of Piper stock between May 14 and May 23. To reach these transactions, the majority would stretch the wording of 10b-6 beyond anything that courts, commentators, and—in published actions—the SEC had considered included until this case.

Rule 10b-6 seeks to prevent the manipulation of the price of shares which are the subject of a current or impending public offering. It is concededly a highly technical rule, and, as the Commission explicitly noted at its adoption, it covers only a limited number of undesirable practices:

> The Rules [10b-6, -7, -8] do not purport to cover every possible type of manipulation or deceptive activity.

> The fact that a particular activity is not specifically dealt with or prohibited in such rules does not necessarily mean that it is not unlawful under the Act or the Commission's other rules.

SEC Securities Act Release No. 5194 (July 5, 1955). The practice particularly condemned is the offering company purchasing its own shares on the market, thereby buoying up the market price close to that set in the public offering. As is so often the case in the field of securities laws, there are a host of other, closely related transactions having the same manipulative effect on the tender offer which are also barred by the Rule. For example, section (b) controls the situation where the offering in prospect involves warrants; there, the issuer cannot purchase those of its shares represented by the rights. It seems to me improper to extend this sort of technical, limited and consistently interpreted rule to a common practice which until now has never been thought within its ambit.

As an original matter, it might be desirable to prohibit a tendering company from purchasing the target company's shares, but the proper way to accomplish this end, taken by the Commission with its new Rule 10b-13, is to adopt a new rule rather than stretch an established one beyond its recognized bounds. The Commission, however, seems not to have been content to wait until 10b-13 became effective to enforce its new policy. Rather, it invoked 10b-6 during the interim by a boot-strap operation, claiming in the release announcing 10b-13 that the proposed rule was "in effect, a codification of existing interpretations under Rule 10b-6. . . ." I sympathize with the Commission's dilemma when, having announced a new policy, it cannot reach current transactions until the new rule becomes effective. But it seems to me that the cost of waiting will rarely be too great as the Commission presumably has lived with the

offending practice for years; it expects us to make bad law to bail it out.

My belief that 10b-6 is being invoked here merely as a stop-gap measure is strengthened by several factors. Although the Commission claims that its position reflects consistent staff practice, I have found no published interpretations, either administrative or judicial, before the Release accompanying proposed Rule 10b-13 that indicate the Commission's view that 10b-6 reaches the shares of a target company. And discussions of the phrase "rights to purchase any such security" and of section 10b-6(b) by the commentators have been directed exclusively to the situations involving two securities of the same company, such as the distribution of a convertible debenture coupled with purchases of the underlying security. *See, e.g.*, Comment, The SEC's Rule 10b-6: Preserving a Competitive Market During Distributions, 1967 Duke L.J. 809, 831; Disclosure Requirements of Public Companies and Insiders 138-42 (Flom, Garfinkel & Freund ed. 1967).

Significantly, the SEC did not see fit to apply its interpretation of 10b-6 to Bangor Punta, although it knew of the May purchases.[4] The final paragraph of the consent

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[4] It may well be that the Commission's course of action was prompted by internal confusion. While Chris-Craft was warned on April 7th that the Commission would consider purchase of Piper stock while its tender offer was pending a violation of 10b-6, no such warning was ever communicated to Bangor Punta. When Chris-Craft abided by this prohibition, the Commission may have felt that its error had given Bangor Punta an inequitable advantage which it ought to seek to correct by the position it has taken in its amicus brief. I do not feel, however, that Bangor Punta—an equally innocent party—should be made to suffer for any failure on the part of the Commission or its staff. In any event, Bangor Punta acted within the law and consistent with the rulings of the SEC with respect to Rule 10b-6.

decree, entered on May 26, does not prohibit Bangor Punta from acquiring Piper stock other than through the exchange offer. Nor did the SEC require Bangor Punta to include an appropriate disclosure in its prospectus, as it clearly had the power to do,[5] of an alleged violation of its Rules, although Bangor Punta did mention the May purchases. Thus, I feel the SEC's own conduct casts doubt on its claim that "the Commission's staff has so construed the rule in similar situations."

Rule 10b-6 has until this case been a limited, highly technical rule. Despite the fact that a change in Commission policy cannot be put into effect for several months because of the procedural safeguards of the Administrative Procedure Act, the Commission now claims that we must reach the same result by accepting its interpretation, i.e., that the rule has meant this all along. I cannot believe that this practice is consonant with the standards of due process and elemental fairness long engrained in the operation of administrative law.

Since I conclude that Bangor Punta's purchases do not fall within the ambit of Rule 10b-6 as consistently interpreted and universally understood as of May, 1969, and I do not believe the May 8th announcement was in violation of the securities laws, I would affirm Judge Tenney's opinion below.

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[5] *See, e.g.*, Northwest Industries Registration Effective, SEC News Digest, Issue No. 69-73 (April 17, 1969).

APPENDIX C

Opinion of Judge Milton Pollack of the United States District Court of the Southern District of New York in *Securities and Exchange Commission* v. *Bangor Punta Corporation*, dated August 25, 1971

C-1

United States District Court

SOUTHERN DISTRICT OF NEW YORK

SECURITIES AND EXCHANGE COMMISSION, *Plaintiff*, *v.* BANGOR PUNTA CORPORATION, *Defendant.*	70 Civ. 3940(MP)

FINDINGS AND OPINION

APPEARANCES:

PHILIP A. LOOMIS, JR., *General Counsel*
DAVID FERBER, *Solicitor*
ROBERT E. KUSHNER, *Assistant General Counsel*
JAMES J. SEXTON, *Attorney*
Attorneys for Plaintiff,
Securities and Exchange Commission
Washington, D. C. 20549

WEBSTER SHEFFIELD FLEISCHMANN HITCHCOCK & BROOKFIELD
Attorneys for Defendant
One Rockefeller Plaza
New York, N. Y. 10020

By: James V. Ryan, Esq. and
C. Kenneth Shank, Jr., Esq. of Counsel

POLLACK, *District Judge.*

Judge Pollack's August 25, 1971 Opinion

POLLACK, *District Judge.*

This is one of a series of cases in this Court arising out of a contest between Bangor Punta Corporation ("Bangor Punta") and Chris-Craft Corporation for control of Piper Aircraft Company ("Piper")—a struggle in which Bangor Punta emerged, in September, 1969, with control of Piper.[1]

Here the Securities and Exchange Commission ("Commission") asks the Court to enjoin Bangor Punta from violating the Securities Act of 1933 and the Securities Exchange Act of 1934 and to order Bangor Punta to make an offer of rescission to holders of Piper stock who exchanged their shares for securities of Bangor Punta, pursuant to an exchange offer of July, 1969.

The Commission charges that Bangor Punta's registration statement and prospectus dated July 18, 1969 pertaining to the Piper exchange offer were materially deficient in omitting to disclose an alleged decision to sell Bangor Punta's 98.7% stock interest in the Bangor and Aroostook Railroad ("BAR") at a price far below its carrying value on Bangor Punta's books and financial statements.[2] The Commission further charges that Bangor Punta intentionally deferred a closing of that sale in order to avoid making and exposing the necessary write-downs until the exchange offer was completed.

Bangor Punta denies that the sale had been decided on in the June to August period that year or that there was

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[1] In *Chris-Craft Corporation* v. *Bangor Punta Corporation* (69 Civ. 2227) Chris-Craft sues for damages alleging that Bangor Punta's victory was due to violations of the securities laws. Piper and Bangor Punta have cross-complained. (69 Civ. 2354 and 69 Civ. 2227)

[2] As noted *infra* the sale of BAR stock took place October 2, 1969 and was for $5 million in cash, a figure some $13.5 million below the carrying value of BAR on Bangor Punta's financial statements.

then a reasonable probability of a sale. It contends that it was not required to make any reference in the prospectus of July 18, 1969 to the sale or to any steps leading to sale.[3]

The evidence adduced upon trial established the following facts.

On or about May 29, 1969 Bangor Punta filed with the Commission a registration statement and prospectus for an offering of its securities to holders of Piper common stock in exchange for their shares of Piper. The registration statement became effective on July 18, 1969 and the prospectus was sent thereafter to all Piper shareholders. On this offering, Bangor Punta obtained 111,628 shares of Piper Aircraft or about 7% of the 1,644,790 shares of Piper Aircraft common stock outstanding.

There is no information in the prospectus suggesting consideration or pendency of a sale in June, July or August, 1959. Bangor Punta did sell its stock in BAR to Amoskeag Corporation ("Amoskeag") on October 2, 1969 at a price of $5 million in cash plus certain contingent payments later described.

The historic cost of BAR's assets, less depreciation and other accounting adjustments and less liabilities was about $29.8 million. However, the financial statements in the prospectus carry Bangor Punta's interest at $18.4 million, a figure which reflects an appraised value of the BAR shares as of September, 1965. The history of this figure is as follows:

Until 1961, BAR was an independent company. It then became a subsidiary of The Bangor and Aroostook Corpo-

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[3] Bangor Punta has alleged affirmatively that the administrative staff of the Commission, to overcome its own errors and shortcomings, has engaged in a course of conduct, the intended result of which has been to interfere on behalf of and to favor Chris-Craft Corporation in its struggle with Bangor Punta for control of Piper, a struggle which has been going on since May, 1969. No proof was adduced to support this contention.

ration (the "Corporation") which had been formed as a holding company. During 1960 and 1961 the Corporation offered its securities to BAR shareholders in exchange for their BAR shares and acquired more than 98% of BAR's outstanding shares. Based on the market price of BAR shares on the New York Stock Exchange before they were delisted in 1961, the Corporation's interest was worth $8.1 million and the Corporation carried the BAR interest at this figure in its financial statements.

In 1964, the Corporation combined with Bangor Punta (a wholly-owned subsidiary of Punta Alegre Sugar Corporation). Although Bangor Punta could have shown its equity in the net assets of the BAR at $29.8 million, it elected to carry forward the figure appearing on the books of the Corporation, viz., $8.1 million. It is claimed that this was done because of a strong possibility that BAR was to be disposed of promptly. By September, 1965 that possibility had evaporated. But, instead of restating the carrying value of BAR at the amount of Bangor Punta's equity interest in BAR on a historical cost basis (which would have resulted in a carrying figure of $29.8 million) or at its or its predecessor's cost, Bangor Punta obtained an appraisal from investment banking houses with knowledge of the railroad industry. Based on their recommendation as to approximate fair market value Bangor Punta restated the BAR holding at $18.4 million—approximately $10 million less than its equity in the underlying net asset value of the railroad on an historical cost basis and $10 million more than the former carrying figure. The difference between the former carrying figure of $8.1 million and the new appraised value of $18.4 million was credited directly to Bangor Punta's earned surplus, by-passing the profit and loss account. This treatment had been the subject of inquiry

by the Commission in connection with a prior registration statement and, after explanations were made, the Commission dropped the matter.

Except for minor accounting adjustments the $18.4 million carrying value of BAR established in 1965 remained unchanged and was reflected in the 1969 registration.

Bangor Punta's management had, for some time, sought a means of separating out BAR in a way which would permit its continued operation as a railroad. Discussions to that end were held within Bangor Punta in 1967 and 1968 and continued into 1969. Several methods were speculated on: viz., the creation of a New England Railroad System by combining the BAR with the Maine Central and Boston and Maine Railroads; an acquisition of the Delaware and Hudson Corporation to combine its railroad with the BAR; a spin off of BAR or a rights offering to the Bangor Punta stockholders. Prior to April of 1969 there seemed to be no prospect of a buyer for the railroad.

On April 1, 1969 Bangor Punta appointed a committee to study the possible divestiture of BAR. The committee consisted of Curtis M. Hutchins, a director and member of the Executive Committee, Gordon Robertson, co-Chairman of the Board and Chairman of the Executive Committee, Robert G. Stone and George H. Siel, Directors of the railroad. Messrs. Hutchins and Robertson were both past presidents of the railroad. This was a highly knowledgeable group on matters pertaining to the railroad and its problems.

Some weeks after the Committee was appointed Amoskeag Company through its president, Frederic C. Dumaine, made an offer to C. M. Hutchins for the railroad of $5 million in cash. Dumaine had long and active experience in the railroad business as an operator. Amoskeag was a

registered investment company with investments in the Maine Central Railroad Company among other enterprises. Dumaine's price was merely the amount of the savings in operating expenses which he estimated could be effected if the Maine Central and BAR were combined.

Hutchins told Dumaine—in response to his query—that Bangor Punta might dispose of its interest in the railroad if the price was right. To Dumaine's offer of $5 million—for either the assets or the stock[4]—Hutchins responded that this was exceedingly low but that he would convey it to the management. Essential details—including the railroad's cash flow figures; its balance sheet and a five year forecast, both cash and profit and loss—were furnished to Dumaine at a second meeting with Hutchins. Dumaine reaffirmed his $5 million offer as his highest price. Hutchins explained that he had no authority except to explore possibilities of divestiture of the railroad; he had no power of decision.

Hutchins and the Committee members with whom he conferred concluded that sale of BAR stock to Amoskeag at the proferred price of $5 million was the "best course for Bangor Punta to pursue."

The company's independent auditors were asked about the accounting treatment which would be afforded a sale of the railroad for $5 million. On May 20, 1969 they reported that such a sale would be treated on the financial statements of Bangor Punta as an extraordinary loss of about $13.5 million.

On May 21, 1969 at a meeting of Bangor Punta's Board of Directors, Hutchins, speaking for all the members of his Committee, stated that there were three possibilities for the

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[4] Dumaine's offer soon narrowed to one for the stock only and remained such through the negotiations.

future of BAR. Bangor Punta might (1) keep the railroad as is, (2) continue to seek to merge it with another railroad, or (3) sell BAR at the best possible price. He discussed each of these possibilities. In respect of the third possibility, he stated that the only person he knew who might be interested in a purchase was Dumaine, of Amoskeag. He reported that preliminary discussions with Dumaine indicated that he might be willing to pay $5 million in cash, securities or some combination of both.

Hutchins told the Board that his Committee unanimously recommended sale at the $5 million price. He reported that over the next five years a heavy infusion of capital in the order of $5 million would be needed to break even from operations. He gave very little hope for the possibility of a merger except conceivably with the Boston and Maine Railroad, and noted that this would produce securities rather than cash for Bangor Punta. This proposal of sale was a surprise to the Board and met with the objection that the Board had insufficient information to make an intelligent decision since a great deal of accounting, tax and legal work had to be done as a preliminary matter to put the offer in proper focus.

In the course of the meeting, counter-suggestions as to price to be sought were broached by the Chairman of the Board, Nicholas M. Salgo.

Following discussion, it was the consensus of the Board that Hutchins should attempt to negotiate for a sale, at book value, of 51% of the stock of BAR and sale of the balance at a higher price with a total consideration to approximate $7 million. Hutchins was separately authorized to negotiate a sale of 100% of the BAR stock, subject to an investigation of the tax and accounting ramifications of such a transaction and subject to the approval of the

Board of Directors or of the Executive Committee of the Board of Directors.

Dumaine, informed by Hutchins of the Board's counter-suggestions, would not change his offer. Dumaine and Hutchins then drafted an unsigned letter setting forth a proposed arrangement of sale which Hutchins was to present to the Board. The draft, reciting that Hutchins was authorized only to explore the situation tentatively and that any "understanding" was subject to approval by the Board of Directors,[5] stated that Hutchins and Dumaine had agreed on the sale to Amoskeag of all the BAR stock owned by Bangor Punta for $5 million plus some additions, subject to ICC approval.

Shortly thereafter, on June 3, 1969, following Hutchins' report to a key management group of Bangor Punta, it was decided to table the entire matter until the tax impact upon Bangor Punta of a sale of assets, as compared with some other disposition of the interest, could be studied and ascertained.[6] Nothing indicated that there was any especial urgency to give the matter earlier consideration. While the divestiture of this asset was a matter of significant interest to Bangor Punta, time was not made of the essence, by either Bangor Punta or Amoskeag.

Two weeks later, on June 16th, Hutchins met with Dumaine and apprised him of the management's decision

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[5] Hutchins explicitly informed Dumaine that time was needed for accountants and tax personnel of Bangor Punta to *review the tax effects of any deal and the evidence unquestionably confirms Hutchins' limited exploratory role.*

[6] The study would require considerable time since it involved going to the Interstate Commerce Commission, sending representatives to Maine and going back over some 70 years of financial history and records and books of the BAR—a time consuming and complex project.

not to approve or accept the unsigned draft letter. He told him that Bangor Punta lawyers and accountants had no time available then to make the investigations and reports deemed essential by the Board; that they were busy with a variety of other matters, including a pending SEC registration statement (the Piper exchange offer); and that it might be two months before they could get to the investigation of the factors material to Bangor Punta's consideration of a sale.

Bangor Punta's general exchange offer for the common stock of Piper Aireraft expired at 5 P.M. on July 29, 1969 and was approved by Bangor Punta's shareholders on August 7, 1969. On August 8, 1969, Bangor Punta commenced distributing its securities to Piper shareholders who had accepted the exchange offer. The final prospectus for the offer stated:

> Until August 27, 1969, all dealers effecting transactions in the registered securities, whether or not participating in this distribution, may be required to deliver a Prospectus.

In the latter part of August, 1969, with the exchange program well nigh completed, Hutchins approached the general counsel of Bangor Punta with the suggestion that the required studies in respect to a sale of BAR go forward. Following instructions from the president, counsel began to gather the information which the Board of Directors was seeking.[7]

On September 9, 1969, Bangor Punta's Board of Directors continued their discussions regarding the sale of BAR, which according to the minutes "has been under

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[7] The president was, however, careful to caution counsel not to allow the inquiry to interfere with any pressing current matters.

the consideration by the Board of Directors for a considerable period of time". Various proposals concerning the sale of the railroad were discussed, including an asset sale, a combination of a partial sale of the assets and a leasing arrangement of the remaining assets, and the sale of the stock of the railroad.

The Directors voted at that meeting to authorize Hutchins to consummate the sale of either the assets or stock of BAR to Amoskeag or to any other buyer for a consideration of $5 million or more in cash and such other additional consideration and benefits as were in his judgment obtainable and the Board authorized the execution of documents and the taking of all other action necessary to consummate a sale in accordance with the terms and conditions so to be negotiated.

Six days later, on September 15, Hutchins wrote to Dumaine that Bangor Punta had not yet reached a decision as to whether it would be most advantageous to dispose of its interest in the BAR through a sale of the stock ownership or in the form of an assets sale. Hutchins proposed to Dumaine that an agreement be worked out which would allow Bangor Punta, at its option, to sell either the BAR stock or assets.

On October 2, Hutchins and Robertson met with Dumaine in Boston. Dumaine refused to change his position in respect of an assets transaction. Thereupon, a contract for the sale of the stock of BAR to Amoskeag was prepared and signed and the closing followed immediately thereafter.

The agreement of sale called for payment of $5 million in cash and other consideration. It was agreed that, if within three years BAR should transfer all of its assets except in a transaction in which neither gain nor loss is recognized for federal income taxes, Amoskeag would pay

Bangor Punta an additional $1.5 million within 30 days after such transfer sale or other disposition.[8] And, subject to specified conditions, Amoskeag agreed that it would also pay the net profits received by BAR within the next five years from sale of all or any part of its property at Sears Island, Maine.

The public announcement of the BAR sale on October 3, 1969 expressly stated that it would result in a non-recurring book loss of approximately $13 million with no tax benefit to the company and that part of the $5 million to be received in cash for the stock would be subject to capital gains taxes.

Major Factual Contentions and Conclusions

It is contended by the Commission—and Dumaine gave testimony supporting the notion—that, at some undefined time during June, July or August, Bangor Punta had decided upon the sale to Amoskeag but decided to defer it to avoid disclosure in the pending registration statement and prospectus. These contentions, as well as Dumaine's testimony on the subject, lack support both in the credible evidence and in the probabilities. Indeed the evidence which the Court accepts as worthy of belief unequivocally negates any such purpose or plan.

The Commission's reliance on Dumaine's testimony is misplaced and the inferences which it has sought to draw that a sale was determined upon and deliberately deferred to avoid disclosure, are not accepted.[9]

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[8] The purpose of this provision is not entirely clear. It may have been intended to act as a deterrent to Amoskeag to consider any course but continuance of operation of the road.

[9] From observation during the trial the Court concludes that both Dumaine and Hutchins who negotiated and desired the sale, believed what they wished to believe, that their personal agreement concluded all but the formalities.

The Bangor Punta Board's behavior was consistent with the dictates of prudence. It insisted on consideration and study of alternatives. It accepted the sale only after being convinced that no viable alternatives existed. If there was a conscious tactical motive in delay, the most believable one is that the Board hoped to let Dumaine (and indeed Hutchins, whose personal commitment to the sale was obvious) simmer long enough to come up with something better. Indeed, even after the Board meeting of September 9, information was being supplied to the Board and, on September 29, some of the Board members attempted to block a sale of stock and bring about a sale of assets. Their reasons were weighty—for a sale of assets might permit the reflection of a tax loss as high as $17.7 million, with some $9 million of cash flow addition for Bangor Punta—as distinguished for the taxability of proceeds from sale of stock.

Thus, while the Court finds that there was an intention to sell, failing other alternatives and upon the best available tax and accounting bases, the Court does not find that Bangor Punta consciously concealed, deferred or refrained from going forward with Dumaine's offer in order to circumvent disclosure in a pending registration statement.

Requirements of Disclosure

Bangor Punta could not in its registration statement and prospectus for the exchange offer omit "to state [any] material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading." Section 17(a) of the Securities Act of 1933, 15 U.S.C. 77q(a); Section 10(b) of the Securities Act of 1934, 15 U.S.C. 78j(b), and Rule 10b-5, 17 CFR 240.10b-5.

Bangor Punta's registration statement became effective on July 18, 1969. It "spoke" as of that date. The duty of

dealers to use prospectuses continued until August 27, 1969.[10] The Commission insists that as of these dates Bangor Punta intended to sell and there was a reasonable probability that it would sell BAR at a substantial loss. Its failure to reflect this state of affairs is claimed to constitute the violations charged.

The Court has found that as of these dates Bangor Punta had not reached a decision to sell. The Commission's charge that the sale was a reasonable probability is made from the vantage point of hindsight. In the total perspective of events preceding the sale—including the last-minute attempts to convert it into a sale of assets—the Court cannot find that the sale was a reasonable probability at the time and to the people involved. *Cf. James Blackstone Mem. Library Assn.* v. *Gulf, Mobile and Ohio R. Co.*, 264 F.2d 445 (7th Cir.), *cert. denied*, 361 U.S. 815 (1959). However, this does not necessarily mean that Bangor Punta met the obligation imposed upon it to make a requisite disclosure under the circumstances of this case. For the circumstances do indicate a sufficiently serious consideration of the possibility of sale at a figure some $13 million below the then carrying value of the BAR stock on Bangor Punta's books so as to force the conclusion that the Bangor Punta directors could not, at the time, have believed that the $18.4 million figure (based on an appraisal of 1965 fair market value) any longer represented a responsible appraisal of market value of the BAR holding.

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[10] The antifraud provisions of the Securities Act (§ 17(a)) and of the Exchange Act (§ 10(b) and Rule 10b-5) require the prospectus to reflect any post-effective changes necessary to keep the prospectus from being misleading in any material respect. This is sometimes handled mechanically by putting a sticker on the prospectus or supplementing it otherwise. The procedure to be used is set forth in 17 CFR 230.424(c).

In this respect, however, the Commission is claiming more than it needs to. The essential question is whether, despite the non-existence of intent or of reasonable probability, the circumstances surrounding the sale were such as to indicate that the $18.4 million carrying figure of the BAR holding was obsolete to the point of being misleading. The Court finds that it was—absent full disclosure of the factors affecting the ultimate decision to sell the BAR interest at a figure of $5 million—or even $7 million—and regardless of whether the sale was to be of stock or of assets.

The Court is aware of no principle of accounting or of fair disclosure which would justify a failure to up-date a constructed carrying figure which may have reflected approximate fair value in 1965 but which was almost four times the offer of a willing buyer (and the only willing buyer) in 1969—an offer which the Board, despite its efforts in good faith to find alternatives—was constrained ultimately to accept. Consistency of fair disclosure required exposure of circumstances which so clearly rendered obsolete an appraisal made four years earlier.

I find that Bangor Punta did not intentionally or purposefully mislead Piper Aircraft stockholders or the public or investors by the omission to make disclosure of the sale under consideration nor did Bangor Punta or its directors intend to gain an advantage over Chris-Craft by the nondisclosure in the contest being waged for control of Piper. There was no purposeful connection between the nondisclosure and the contest for control. In other words, the nondisclosure was not prompted by an improper purpose. However, absence of bad faith does not excuse the failure to state facts necessary to make the facts stated not misleading.

The explanatory footnote which did appear on the 1969 balance sheet was given so that anybody looking at the

financial statements would not be confused as to why the full equity of the railroad was not picked up by Bangor Punta as the carrying value of its investment. By the same token, the 1965 constructed carrying value should not have been used when it was known to substantially exceed the only bid that could be generated from a purchaser capable and willing to buy and operate the asset.

Bearing on Exchanging Piper Holder

The standard of materiality to be applied here is whether a reasonable stockholder of Piper might have hesitated to make an exchange for Bangor Punta securities with such a large loss figure emerging—at least until sufficiently explained and put in proper perspective, in terms understandable by a reasonable investor.

At the end of fiscal 1968, Bangor Punta had retained earnings of $37.9 million. A sale of the stock at $5 million would result in a book loss equivalent to 36.5% of such retained earnings.

At the end of fiscal 1968, the shareholders' book equity in Bangor Punta was $113.5 million and a sale of the BAR at $5 million would result in a loss of 12% of the shareholders' book equity.

Bangor Punta had reported profits for each of the five years ending with that for September 30, 1968. A sale such as was being investigated would involve the loss ($4.32 per share) which would have far exceeded the company's net income for any of the five prior years.

The Court concludes that the registration statement and prospectus of Bangor Punta relating to the Piper exchange offer was misleading in its failure to disclose the circumstances surrounding the negotiations for sale of the BAR interest. In so holding especial note is taken of the

unique "valuation" nature of the $18.4 million figure at which the BAR interest was carried on Bangor Punta's books. The present conclusion is not necessarily to be taken as applicable in cases where book carrying figures are in accordance with principles of conventional transactional accounting or where circumstances might otherwise be different.

Relief to be Granted

The Commission has requested an order requiring Bangor Punta to offer rescission to shareholders who accepted the Bangor Punta exchange offer and an order enjoining Bangor Punta from further violations of the securities laws. The Court grants the first and denies the second of these requests.

Bangor Punta claims that such an offer of rescission would be an empty exercise since the Bangor Punta securities received by the Piper shareholders have a market value far in excess of the Piper shares given up by them. See *Electronic Specialty Co.* v. *International Controls Corp.*, 409 F.2d 937, 947 (2d Cir. 1969). The decision whether to rescind is nonetheless one to be made by those who took the exchange.

Accordingly, Bangor Punta will be required to make an offer of rescission and the parties are directed to submit an appropriate decree for the Court's consideration to carry out such an offer. Such offer should allow Bangor Punta full scope to point out any factual considerations bearing on a decision to accept or by-pass rescission as may be accurate and appropriate under the circumstances.

Bangor Punta claims that an injunction is unnecessary and inappropriate since there is no evidence of its bad faith; that it acted on advice of counsel and of its account-

ants; and that this was an isolated transaction involving a single unintentional violation. *Securities and Exchange Commission* v. *Torr,* 87 F.2d 446 (2d Cir. 1937). Moreover, Bangor Punta contends that its past conduct does not indicate a reasonable likelihood of future violations. *Securities and Exchange Commission* v. *Franklin Atlas Corp.,* 171 F. Supp. 711 (S.D.N.Y. 1959) (Dawson, J.); *Securities and Exchange Commission* v. *Texas Gulf Sulphur Co.,*_____ F.2d _____ (2d Cir. June 10, 1971).

The Commission insists that Bangor Punta has demonstrated a propensity for violating the securities law because the company allegedly violated a consent decree entered on May 26, 1969 by the United States District Court for the District of Columbia in the Commission's suit there against Bangor Punta, by filing a registration statement which omitted to disclose the facts discussed in this opinion. That suit centered on a Bangor-Punta-Piper release of May 8, 1969. Bangor Punta consented to the decree and the Commission's complaint here avers that the company's demonstrated propensity for violating the securities laws is not at all based upon the issuance of that release (which is a subject of controversy in an action by Chris-Craft against Bangor Punta and others). *Chris-Craft Industries, Inc.* v. *Bangor Punta Corp.,* 426 F.2d 569, 573-576 (2d Cir. 1970) and *ibid* 69 Civ. 2354 now before this Court for decision.

Under all the facts and circumstances in this case, the Commission has failed to carry its burden to establish, with persuasive evidence, that Bangor Punta, its officers, directors and employees have a propensity or natural inclination to violate the securities law. *Securities and Exchange Commission* v. *Texas Gulf Sulphur Co.,* _____ F.2d ____ (2d Cir. June 10, 1971). Accordingly, the requested injunction is denied.

The foregoing shall constitute the findings and conclusions required by F. R. Civ. P. 52(a).

Submit decree in accordance with these findings on 15 days notice.

So Ordered.

Milton Pollack
U.S. District Judge

August 25, 1971

APPENDIX D

Memorandum Opinion of Judge Milton Pollack of the United States District Court of the Southern District of New York in *Securities and Exchange Commission* v. *Bangor Punta Corporation*, dated September 17, 1971

United States District Court

SOUTHERN DISTRICT OF NEW YORK

SECURITIES AND EXCHANGE COMMISSION, *Plaintiff*, *v.* BANGOR PUNTA CORPORATION, *Defendant.*	70 Civ. 3940(MP)

MEMORANDUM

POLLACK, *District Judge.*

Bangor Punta requested the Court to reopen the record and to make additional findings of fact. Subsequent to receiving SEC's opposition to the request, Bangor Punta withdrew the application to reopen the record as unnecessary and has substituted a request that the Court issue a statement in disposing of this matter that generally accepted accounting principles were not litigated herein. The request and opposing paper are being filed herewith.

It is beyond the scope and intent of the opinion of August 25, 1971 to consider or decide what constitute accepted principles of accounting in the abstract. The opinion deals solely with the requirements of a prospectus used on an exchange of securities and what is to be considered misleading in connection therewith. Any differences between accepted principles of accounting and fair disclosure in a prospectus must be resolved in favor of the disclosure requirements of a prospectus which essentially are a management not an accountant's responsibility.

The application to reopen the record and for additional findings is accordingly denied.

SO ORDERED.

(ORIGINAL SIGNED)
MILTON POLLACK

U. S. District Judge

September 17, 1971

APPENDIX E

Memorandum of Settlement of Judgment of Judge Milton Pollack of the United States District Court of the Southern District of New York in *Securities and Exchange Commission* v. *Bangor Punta Corporation*, dated November 17, 1971

United States District Court

SOUTHERN DISTRICT OF NEW YORK

SECURITIES AND EXCHANGE COMMISSION, *Plaintiff,* *v.* BANGOR PUNTA CORPORATION, *Defendant.*	70 CIV. 3940 (MP)

MEMORANDUM ON SETTLEMENT OF JUDGMENT

POLLACK, *District Judge.*

A provision has been inserted in the decree submitted for settlement requiring that any rescinding holder should account on the offer of rescission for any profits realized from interim sale of all or any part of the original stock obtained on the exchange in August, 1969.

The purpose of restitution is to put the injured party in as good (not a superior) position as that occupied by him before the contract or sale or exchange was made. If a rescinding party has made profitable use of the subject of the rescission, or has received fruits such as dividends or interest or other benefits thereon, these profits, fruits, other benefits and their values must be accounted for by the rescinding party to effect a return to the *status quo ante.* A party will not be permitted to retain the benefits or fruits of a contract and at the same time repudiate it. It is inappropriate for a rescinding party to in effect affirm his ownership in part and to disaffirm the entire transaction.

It is a prerequisite to restitution that a party disgorge to the other party any proceeds the former has received

upon disposition of the original property. *Marr* v. *Tumulty*, 256 N.Y. 15, 175 N.E. 356 (1931).

Mott v. *Tri-Continental Financial Corp.*, 330 F.2d 468, 470 (2d Cir. 1964).

Ordinarily, if one no longer owns the original shares acquired in a rescindable transaction, he is limited to an action for damages and may not be accorded rescission. *Mott* v. *Tri-Continental Financial Corp., cit. supra*, at 470. Equity may waive this requirement in a proper case and may permit the rescinding party to account to the other party for the value of any part sold. Williston, *Contracts*, § 1463, p. 161 (3rd ed., Vol. 12, 1970). Equity may also permit the restitution to consist of substitute shares acquired for the purpose of rescission. In that event, everything of value including the profit, if any, realized from a prior sale or disposition of the original stock and the subsequent reacquisition of like shares must be accounted for to the other party as a prerequisite to rescission, in the same way as other fruits of the interim ownership must be restored. See, Corbin on *Contracts* §§ 1114-1115, Volume 5 (1964 Ed.); 17 Am. Juris. 2d § 512, p. 996 (2d Ed. 1964); *Marr* v. *Tumulty*, 256 N.Y. 15, 175 N.E. 356 (1931); *Ufland & Co.* v. *McMahon*, 215 App. Div. 267, 269 (4th Dept. 1926); *Commissioner of Banks* v. *Chase Securities Corp.*, 298 Mass. 285, N.E. 2d 472, 499, 500 (1937); *E.T.C. Corp.* v. *Title Guar. & Trust Co.*, 271 N.Y. 124, 2 N.E. 2d 284 (1936).

November 17, 1971

MILTON POLLACK
U. S. District Judge.

APPENDIX F

Opinion of Judge Milton Pollack of the United States District Court of the Southern District of New York in *Bangor Punta Corporation* v. *Chris-Craft Industries, Inc. et al.*, dated December 10, 1971

F-1

United States District Court

SOUTHERN DISTRICT OF NEW YORK

BANGOR PUNTA CORPORATION, *Plaintiff,* *v.* CHRIS-CRAFT INDUSTRIES, INC., *et al,* *Defendant.*	69 CIV. 2354 (MP)

OPINION

APPEARANCES:

WEBSTER SHEFFIELD FLEISCHMANN HITCHCOCK & BROOKFIELD
Attorneys for Plaintiff
One Rockefeller Plaza
New York, N. Y. 10020
By: James V. Ryan,
William L. D. Barrett and
C. Kenneth Shank, Jr., Esqs. of Counsel.

PAUL, WEISS, RIFKIND, WHARTON & GARRISON
Attorneys for Defendants
345 Park Avenue
New York, N. Y. 10022
By: Arthur L. Liman,
Joseph J. Ackell and
Jack C. Auspitz, Esqs. of Counsel.

POLLACK, *District Judge.*

F-2

Judge Pollack's Opinion in Bangor Punta Action

POLLACK, *District Judge.*

This cross action by Bangor Punta, a defendant in *Chris-Craft* v. *Bangor Punta et al* (S.D.N.Y. 69 Civ. 2227) decided this day, arises out of the bitter struggle between the two companies for control of Piper Aircraft Corporation. That struggle ended in the marketplace with Bangor Punta in control and continues in the complaints and cross complaints by the parties against each other arising out of their competition.[1]

The principal facts are set out in this Court's opinion in S.D.N.Y. 69 Civ. 2227. They will be deemed incorporated and need not be repeated at length here.

Chris-Craft sued for damages as the losing contender for control of Piper by reason of Bangor Punta's alleged wrongful acts. Bangor Punta countered by charging, in essence, that because of the wrongful acts of Chris-Craft it paid more than it would otherwise have paid to acquire control of Piper. Both suits were tried together.

Bangor Punta adduced no proof specifically in its case as plaintiff. It seeks support for its contentions in the record developed in *Chris-Craft* v. *Bangor Punta, et al.* (S.D.N.Y. 69 Civ. 2227).

This complaint, like that in the companion case, is replete with charges of breach of the requirements of securities laws and rules. Like the other, it has been brought and tried as though any such breach by a competitor automatically creates windfalls for a sophisticated and well-financed contender for corporate control. It must be remembered that this is an action by the willing and winning contender which bought Piper stock with its eyes open, presumably paying what it deemed control of Piper to be

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[1] Piper, the target company, asserted a counter claim against Chris-Craft in S.D.N.Y. 69 Civ. 2227.

worth. The Court has here been especially challenged to maintain its footing in the realities and the equities in searching (in vain) for credible evidence establishing causal connections between alleged violations and actionable damage.

The Contentions

(a) Bangor Punta insists that the plan of Chris-Craft to acquire control of Piper existed before the time when, according to Chris-Craft, the plan was formulated and that Chris-Craft concealed its true purpose from a registration statement filed with SEC to raise capital for the purchase and from prospectuses legally required to be used during a period when its unrevealed plan to obtain control of Piper was in existence.

We comment here on this contention because it is typical of others in the case. Even if it rested on more than mere surmise, it raises no issue proper to a plaintiff in Bangor Punta's posture. Bangor Punta was not a purchaser of securities issued under the statement of which it complains. There are possible links of relevance between the alleged deficiency in the registration statement and Bangor Punta's campaign. But they are not links to liability of Chris-Craft to Bangor Punta. Thus:

(1) If the registration statement were materially misleading there might be room to argue that Chris-Craft obtained by illegal means the money used to compete with Bangor Punta. There might then be examined the rights of those from whom the money was so obtained. But the Court sees no basis for awarding damages to Bangor Punta because Chris-Craft failed to disclose to its sources of funds its intended use of those funds.

(2) If Chris-Craft did intend to use the proceeds of this registered issue to obtain control of Piper, a disclosure of

that fact would have given Piper (and/or Bangor Punta) an earlier opportunity than they had in fact to prepare a counter-campaign. However, Chris-Craft owed no duty to Piper or Bangor Punta to announce its intentions for their benefit. Its disclosure obligations (assuming they existed as alleged) in the prospectus complained of or in 13-D reports, were for the benefit of investors with whom Chris-Craft would be dealing in its campaign for control.[1A] Bangor Punta does complain of failure to make—and of inadequate—13-D statements. Thus:

(i) It asks us to find that Chris-Craft and the broker it used to buy Piper stock constituted a "group" or "syndicate" whose intentions should have been reported.

(ii) It contends that 13-D statements made by Chris-Craft should have disclosed that (as alleged by Bangor Punta) cash used in Chris-Craft's tender offer was borrowed and that such use of the cash would constitute a default under certain of Chris-Craft's arrangements with its creditors.

The first of these contentions is not only far-fetched, but is wholly out of Bangor Punta's reach as a weapon against Chris-Craft. The latter contention would be a dubious one even if made by a Piper stockholder to whom the statement is specifically addressed. For that stockholder either tenders and walks off with cash or remains a Piper holder having no concern with Chris-Craft's relations with its creditors.[2]

[1A] See, *GAF Corporation* v. *Milstein*, 324 F.Supp. 1062 at 1070 (S.D.N.Y. 1971) (Pollack, J.) "the Williams Bill concentrated on an investor protection goal rather than on providing protection for management's ability to repel raiders."

[2] The situation is not the same, of course, in a registration statement covering an offer of exchange. There the accepting holder of target company stock is destined to become an investor in the offering company—with a strong interest in that company's relations with its creditors.

(b) Bangor Punta alleges that Chris-Craft opened a "secret" "numbered" account at a brokerage firm which assisted it in locating and acquiring large institutionally held blocks of Piper. At least one institution (Technology Fund) it is claimed, to which Chris-Craft paid $65 per share for more than 100,000 shares of Piper—at a time when the market was in the low fifties—simultaneously made a large purchase of Chris-Craft stock in the open market. The alleged purpose of this allegedly pre-arranged move was to "stabilize or manipulate" the price of Chris-Craft common. Chris-Craft planned to include in its acquisition program an offer of exchange of Chris-Craft for Piper securities. Obviously, a high price for Chris-Craft common would greatly facilitate such an exchange.

(c) Several other institutions (one of which had tendered Piper stock to Chris-Craft for cash during the pendency of a Chris-Craft tender offer) also bought large amounts of Chris-Craft on the open market. In the month shortly before Chris-Craft filed its registration statement to cover its proposed exchange offer, these institutions purchased some 231,800 Chris-Craft shares (more than 17%) of the number outstanding. These purchases caused the daily average of trading on the New York Stock Exchange to increase from 7,500 shares to 23,400 shares. The price of Chris-Craft common, during this month, rose to 45% above the average of its closing prices for the six weeks preceding these purchases.

By mid-1970, with the serious market decline notably in prices of stocks of conglomerates, the institutions were taking heavy losses. Their liquidations of position, Bangor Punta claims, were designed to do the least damage to the price of Chris-Craft and hence to the progress of Chris-Craft's exchange offer program.

(d) While its cash tender offer for Piper stock was open Chris-Craft was also buying Piper stock in the open market. This was a violation of S.E.C.'s Rule 10b-6 and the Commission, upon becoming aware of what was happening, ordered Chris-Craft to cease these purchases. Thereupon at least one institution (which had previously sold a large block of Piper to Chris-Craft) purchased Piper stock in the open market and tendered the shares to Chris-Craft. Bangor Punta claims the transaction to be a device to have done by others what Chris-Craft could not do itself.

Bangor Punta bottoms its case on Rule 10b-5 under the Securities Exchange Act,[3] claiming that Chris-Craft's "integrated" bid for control of Piper was in its entirety a "manipulative and deceptive contrivance" whose total effect was to inflate the price of Piper stock and so to damage Bangor Punta as a purchaser of that stock. It cites *Eagle* v. *Horvath*, 241 F. Supp. 341, 344 (S.D.N.Y. 1965) for the proposition that while a thoroughly legal campaign by Chris-Craft for control of Piper might also have raised the price of Piper stock, it must make restitution for having done the same thing by illegal means.[4] It cites other cases

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[3] 17 C.F.R. § 240.10b-5 (1971)

[4] *Horvath* and apposite cases, if at all applicable here, are in an important sense contrary to Bangor Punta's position. Bangor Punta asks us to regard the entire Chris-Craft program as fatally tainted because of alleged violation spots in the program. It does not bear the burden of showing the causal relation between the violations themselves and its damage. Yet, the holding in *Horvath* is precisely that such a relation is a vital issue. In *Horvath* a motion for summary judgment in a stockholders' suit was denied because there was, at issue, the question whether an alleged false prospectus in fact motivated stockholder votes on the plan being attacked in the case.

We did not, at Chris-Craft's instance, spread the taint of single alleged violations by Bangor Punta over all of Bangor Punta's campaign. We see no warrant for a contrary treatment of Bangor Punta's contentions here.

for the propositions that privity between buyer and seller is not an essential condition for application of Rule 10b-5, *Fischman* v. *Raytheon*, 188 F.2d 783, 786 (2d Cir. 1951)[5] and that manipulative activities unrelated to the plaintiff and not designed to induce the plaintiff to buy or sell are, nonetheless, actionable. *Cochran* v. *Channing Corp.*, 211 F. Supp. 239 (S.D.N.Y. 1962);[6] *Sarlie* v. *E. L. Bruce Co.*, 265 F. Supp. 371 (S.D.N.Y. 1967).[7] Characterizing itself as a buyer of Piper "deceived" by the manipulative activity of Chris-Craft, Bangor Punta also invokes *Crane Co.* v. *Westinghouse Air Brake Co.*, 419 F.2d 787 (2d Cir. 1969)[8], *cert. denied*, 400 U.S. 822 (1970).

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[5] In *Fischman*, the court (Frank, C. J.) pointed out the difference in proof required to sustain a Section 11 suit under the Act of 1933 and a Section 10-b suit under the Act of 1934. In the former the plaintiff's burden is to show an acquisition of the direct subject of a registration statement while in the latter, any deceived purchaser relying on a *fraud* may sue.

[6] *Cochran* v. *Channing* was a suit by a holder of Agricultural Insurance Company stock who sold at depressed prices and alleged that Channing Corporation, the defendant, dominated the Company, formed an undisclosed plan to secure control of it by offering an exchange of stock of another company for Agricultural and by purchasing Agricultural stock at depressed prices caused by lowering Agricultural's dividend and other similar practices. Judge Dawson of this District held the complaint good under Rule 10b-5 against a motion to dismiss for lack of privity. The case cannot support the contentions of a plaintiff in Bangor Punta's posture. It cannot claim itself a beneficiary of any fiduciary obligation of Chris-Craft such as was deemed by Judge Dawson to be owed by Channing to the plaintiff.

[7] *Sarlie* v. *Bruce* seems wholly inapposite. It involved a default dismissal of plaintiff's action and concerned itself largely with the measure of damages in a counterclaim by a company (Bruce) whose president (Gilbert) allegedly used misappropriated funds in an attempt to capture control of Celotex Corporation.

[8] *Crane* v. *Westinghouse*, is beside the mark. There, the alleged market manipulation was effected for the express purpose of preventing

Other aspects of Chris-Craft's program are complained of—quite apart from their place in an overall scheme alleged to be unlawful.

1. The allegedly induced purchases of Chris-Craft common by institutions preceding the Chris-Craft exchange offer are alleged to be manipulations in violation of Section 9(a)(2) of the Exchange Act[9] which inflated the price of Piper common, as well as that of Chris-Craft. *Crane, supra,* is cited as authority for Chris-Craft's liability.

2. Bangor Punta has reached into the Investment Company Act of 1940, 15 U.S.C. § 80a-1 *et seq.*, in its search for deficiencies in Chris-Craft's program and purports to have found one in Section 17(a), 15 U.S.C. § 80a-17(a) (1971) of that Act. The Section (together with relevant Section 2(a)(3), 15 U.S.C. § 80a-2(a)(3)) provides that without an express order of S.E.C.

> SEC. 17(a) It shall be unlawful for any affiliated person or promotor of or principal underwriter for a registered investment company (other than a company of the character described in Section 12(d) (3)(A) and

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a competitor for control from succeeding in its bid and the facts pleaded showed a distinct causal nexus between the manipulation and its actual and intended result. To suggest that Chris-Craft, itself an avid buyer of Piper, "manipulated" the price of Piper upward and to characterize Bangor Punta as a buyer "deceived" by this manipulation strains even credulity.

[9] Section 9(a)(2), 15 U.S.C. § 78i(a)(2)(1971), reads:

"It shall be unlawful for any person, . . . to effect, alone or with one or more other persons, a series of transactions in any security registered on a national securities exchange creating actual or apparent active trading in such security or raising or depressing the price of such security, for the purpose of inducing the purchase or sale of such security by others."

(B)), or any affiliated person of such a person, promoter, or principal underwriter, acting as principal . . .

(2) knowingly to purchase from such registered company, or from any company controlled by such registered company, any security or other property (except securities of which the seller is the issuer) . . .

SEC. 2(a)(3) "Affiliated person" of another person means (A) any person directly or indirectly owning, controlling, or holding with power to vote 5 per centum or more of the outstanding voting securities of such other person; (B) any person 5 per centum or more of whose outstanding voting securities are directly or indirectly owned, controlled, or held with power to vote, by such other person; . . .

Since, at the time Chris-Craft made its purchase from Technology Fund, *supra*, both it and the Fund owned more than 5% of Piper, Chris-Craft was an affiliate of an affiliate of an investment company and prohibited from making the purchase without prior order of SEC. No such order was ever requested.

The Merits of the Contentions

Chris-Craft's response to Bangor Punta's charges is to label Bangor Punta's case as "sheer fantasy" and its inferences as "Kafkaesque logic". Chris-Craft's attacks on the evidentiary underpinning and legal support of Bangor Punta's case would require a minute consideration of the record and of precedents cited were this Court to accord to Bangor Punta the status of damaged innocent which it claims for itself.

But Bangor Punta cannot wear that mantle. It was the willing and winning contestant in a hard fought and (for both sides) enormously expensive struggle for control.

Judge Pollack's Opinion in Bangor Punta Action

This Court will readily agree that Bangor Punta paid more to acquire control of Piper than it would have if Chris-Craft had not, by the time Bangor Punta entered the contest, already been well on its way in acquiring Piper stock. Indeed the possibilities are that, if Chris-Craft had not already shown itself to be so powerful a bidder for control, Bangor Punta's cost would have been zero. For the record is ineluctably convincing that Bangor Punta came in at Piper's urging and specifically to resist Chris-Craft.

In dealing with *Chris-Craft* v. *Bangor Punta et al., supra,* this Court made it clear that it would not, at the behest of a disappointed contender in a battle for corporate control, necessarily take the same view of the requirements of the securities laws and rules as it does in cases of claimed injury to the average public investor. These considerations apply with even greater vigor to actions by the winner complaining that he was forced to overpay.

Bangor Punta's claim of "integrated" and "concerted" efforts by "coparticipants" has no more weight than similar language aimed by Chris-Craft, as plaintiff, against Bangor Punta as defendant. Chris-Craft has amply disposed of several of Bangor Punta's factual contentions (as e.g., its charge that an originally submitted and then deleted portion of Chris-Craft's registration statement to cover its debenture issue in December 1968 "evidenced" an undisclosed intention to acquire Piper with the proceeds). But even taking on their face each of Bangor Punta's charges of violations leaves us asking why Bangor Punta should be made a money beneficiary. The price it paid for Piper it paid with open eyes. The rapport between it and the Piper management should have given it more easy access to information about Piper than was available to Chris-Craft—even with two Chris-Craft representatives on the

Piper board. Its inducement to pay the prices it did for Piper control was not in any one or combination of the violations it seeks to lay at Chris-Craft's door step. The inducement was its own determination to have control.[10]

However, even if Bangor Punta were an apt plaintiff to raise the shield of the securities laws and rules for its protection, this Court would have great difficulty in finding—on facts and law—that a convincing case has been made out. Bangor Punta did not carry its burden of persuasion on the issues presented in its case against Chris-Craft. Its basic claim that Chris-Craft "manipulated" upward the price of Piper stock asks us to assume that Chris-Craft massaged the market against its own interest—since Chris-Craft was in an acquisition campaign—and that Bangor Punta, amply aware of what Chris-Craft was doing and bidding Chris-Craft up, was somehow victimized by this massaging.[11] The claim is patently untenable. Its claim that purchases of Chris-Craft common by institutions were arranged for manipulative or evasive reasons are

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[10] The disposition of this case and of *Chris-Craft* v. *Bangor Punta et al.*, S.D.N.Y. 69 Civ. *2227* eliminates any requirement for findings as to damages. Were such findings necessary, this Court could give no weight to the unsubstantiated and cursory evidence presented on behalf of Chris-Craft. On the other hand, the careful and well-documented analysis presented by the expert for Bangor Punta was persuasive in the main on the issue of fair market value of Piper stock in or about May, 1969 during, but uninfluenced by, the contest for control and fair market value uninfluenced by extraneous factors at the time of the trial herein in March, 1971.

[11] The willingness of an innocent buyer to pay a manipulated price does not deprive him of a right to complain of the manipulation. But the essence of a manipulation is the execution of transactions affecting prices or actual or apparent market activity for the purpose of inducing others to buy or sell. While Chris-Craft's initial and subsequent bids raised the prices of Piper stock these bids were for the *bona fide* purpose of acquiring stock for itself, not to induce others to buy the stock.

pure surmise—such basis as they do have is purely circumstantial and lacks the persuasive power needed to support such charges. The charge that in disposing of Chris-Craft holdings the institutions acted to produce the least possible disturbance of price does no more than charge the institutions with ordinary prudence in their management of their affairs.

The charge of violation of Section 17(a) of the Investment Company Act, 15 U.S.C. § 80a-17(a)(1971) has some surface plausibility but as little substance as the others. That section can apply to the Chris-Craft-Technology Fund transaction only upon a most abstrusely technical reading. It is not clear whether the mechanics of transfer and delivery and the "as of" dates for voting of Piper stock at a forthcoming meeting were such as to truly vest in Chris-Craft voting power for its 5% plus holding in Piper at the time. Even if it did have that power, the record before this Court is convincing that Chris-Craft, did not then or thereafter, exercise any controlling influence in Piper. Section 17(a) was designed to protect an investment company in its transactions with affiliates. In view of the price received by the Technology Fund ($65 per share as against the then market in the low fifties) and of subsequent events, it is difficult to discern any harm to the Fund in its sale of Piper stock to Chris-Craft. Bangor Punta is, under the circumstances, well beyond the pale of protection fairly intended by Section 17(a) of the Investment Company Act.

Bangor Punta's charges, compiled by able and diligent counsel, are an illuminating catalogue of pitfalls in the path of a contender for control of an unwilling target, competing with a well-financed adversary. However, the diligence is misplaced. The alleged breaches must not only be supported by credible evidence but must, importantly, be

causally linked to damages. The complaint falls short on both scores.

The complaint is dismissed for failure to sustain with credible evidence, the burden of proof cast upon the plaintiff.

The foregoing shall constitute the findings and conclusions required by F. R. Civ. P. 52(a).

So Ordered.

(original signed)

Milton Pollack
U. S. District Judge

December 10, 1971

APPENDIX G

Opinion of Judge Milton Pollack of the United States District Court of the Southern District of New York in *Chris-Craft Industries, Inc.* v. *Piper Aircraft Corporation, et al.*, dated December 10, 1971

United States District Court

SOUTHERN DISTRICT OF NEW YORK

CHRIS-CRAFT INDUSTRIES, INC., *Plaintiff*, *v.* PIPER AIRCRAFT CORPORATION, *et al.*, *Defendants.*	69 CIV. 2227 (MP)

OPINION

APPEARANCES:

PAUL, WEISS, RIFKIND, WHARTON & GARRISON
Attorneys for Plaintiff
345 Park Avenue, New York, N.Y. 10022

By: Arthur L. Liman,
Joseph J. Ackell and
Jack C. Auspitz, Esqs., of Counsel

WEBSTER SHEFFIELD FLEISCHMANN HITCHCOCK & BROOKFIELD
Attorneys for Defendants (Bangor Punta Corporation, Nicholas Salgo and David W. Wallace)
One Rockefeller Plaza, New York, N.Y. 10020

By: James V. Ryan,
William L. D. Barrett and
C. Kenneth Shank, Jr., Esqs., of Counsel

Judge Pollack's Opinion in Chris-Craft Action

CHADBOURNE, PARKE, WHITESIDE & WOLFF
Attorneys for Defendants (Piper Aircraft Corporation, William T. Piper, Jr., Howard Piper and Thomas F. Piper)
25 Broadway, New York, N.Y. 10004

By: Paul G. Pennoyer, Jr.,
Zachary Shimer and
Irene C. Warshauer, Esqs., of Counsel

SULLIVAN AND CROMWELL
Attorneys for Defendants (The First Boston Corporation, Paul L. Miller and Nicholas A. Bayard)
48 Wall Street, New York, N.Y. 10005

By: John F. Arning,
Roger L. Waldman and
Charles W. Sullivan, Esqs., of Counsel

POLLACK, *District Judge:*

The Context of the Case

This case and its companion cases[1] arise out of the unsuccessful attempt of Chris-Craft Industries, Inc. (Chris-Craft), a diversified manufacturer of recreational products, to secure control of Piper Aircraft Corporation (Piper), a leading manufacturer of light aircraft. The Chris-Craft takeover attempt was resisted by Piper and by a competitor for the control, Bangor Punta Corporation (Bangor Punta), which eventually succeeded in acquiring more than 50% of the outstanding Piper shares. The bulk of Chris-

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[1] *Bangor Punta* v. *Chris-Craft*, U.S.D.C. S.D.N.Y., 69 Civ. 2354 (MP), which is being decided this day; and *SEC* v. *Bangor Punta, et al.*, 331 F. Supp. 1154 (S.D.N.Y. 1971) (Pollack, *J.*).

Craft's complaints is based on charges that Bangor Punta's success was achieved and Chris-Craft's failure and its asserted damages were caused by deception of the Piper shareholders and of Chris-Craft in violation of various provisions of the federal securities laws and regulations.

Only a minor segment of the case involves charges that Chris-Craft was directly deceived by Piper. The balance of the case deals with charges of deceptions alleged to have been committed by Piper and Bangor Punta on public holders of Piper stock to induce them not to accept Chris-Craft's offers to acquire their stock by purchase or exchange. Chris-Craft claims also that Bangor Punta privately acquired three critical blocks of Piper stock during the pendency of an exchange offer in violation of an SEC Rule.

The contest for control of Piper was sophisticated and hard fought. The contenders were men accustomed to the handling of vast sums of public capital, were assisted by skilled professionals and were themselves seasoned in corporate tactics. It is not hard to detect personal overtones which added some passion and urgency to the contest. In addition, the conduct of both sides invoked the attention of the SEC and the New York Stock Exchange.

Thus, neither side can approximate itself to the position of an average public investor for whose express benefit, in dealing with others of superior knowledge (or the capacity to gain it), skill and resources, the law was designed. The Court does not intend to imply that contests for corporate control are to be unmediated by standards properly applicable under common law, federal legislation or regulation. However, substantial justice cannot be done by mere mechanical application of standards evolved to correct the imbalances of knowledge, skill and capacity for self-

protection which so often occur in securities transactions between members of the public and professionals. Nor can the Court be indifferent to the ultimate source from which the damages are claimed, in effect. (See *infra*, 35-37).

The Major Events

Piper stock was listed on the New York Stock Exchange. There were 1,641,890 shares outstanding. Chris-Craft began purchasing Piper stock just before the end of 1968. By January 21, 1969 Chris-Craft had acquired 102,600 shares of Piper stock on the New York Stock Exchange. On the next day it increased its holdings by purchasing 101,100 shares at $65 per share from Technology Fund, a midwest-based mutual fund; this made Chris-Craft's holdings total 13% of the issue. The market for the stock was then in the low fifties. On January 23, 1969, Chris-Craft announced a cash tender offer for Piper shares of $65 per share and it obtained 304,606 shares through tenders. It also bought an additional 38,000 shares approximately bringing its holdings by February 3, 1969, to 547,106 shares, a number barely short of one-third of the shares outstanding, at a cost of $34,677,000.

The Piper management (in essence the Piper family), which held some 31% of the outstanding Piper stock, reacted to the Chris-Craft tender offer by a communication to shareholders late in January to dissuade them from accepting the Chris-Craft tender offer. One of its statements complained of by Chris-Craft was that the Piper management considered the Chris-Craft $65 tender price inadequate. Chris-Craft charges that this was a misleading statement, based on the facts that Piper's investment bankers, First Boston Corporation, had advised Piper that a $65 price was fair and, furthermore, that on January 29, Piper had announced an agreement to sell 800,000 unissued Piper shares to Grumman Aircraft Company at $65 per

share.[2] The Grumman agreement was not consummated and the additional shares were not issued.

On February 27, Chris-Craft filed with the Securities and Exchange Commission ("Commission") an S-1 registration statement as a step in a proposed offer of exchange of a Chris-Craft package of securities for Piper stock. (The statement did not become effective until May 15.)

On March 22, Piper issued 469,199 authorized but unissued shares to acquire control of two companies, viz., Southply, Incorporated and United States Concrete Pipe Company of Florida. Apart from increasing the number of shares outstanding, these acquisitions could make Piper less attractive to Chris-Craft since the Pipe Company was not in the recreational field and ownership of Southply, a speedboat manufacturer, might bring Chris-Craft into conflict with antitrust law. However, Piper rescinded both of these acquisitions within a short time. Piper had failed to comply with its listing agreement with the New York Stock Exchange by issuing such a block of shares before seeking the approval thereof of its stockholders. This omission led the Exchange to refuse the listing of the newly issued shares, to suspend trading in all Piper shares on the Exchange and to initiate delisting proceedings.

Following the rescission of both of these acquisitions, the Piper family revived negotiations with Bangor Punta, begun early in January, toward securing a defensive merger between Piper and Bangor Punta.

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[2] Part of the agreement, not mentioned in the announcement, was an option in Grumman to "put" the shares back to Piper after six months at Grumman's cost plus interest. Piper insists that the "put" was part of an overall understanding that the proposed sale was a step in a possible Grumman-Piper merger, failing which Grumman might not be interested in a holding of Piper stock. The "put" was described in Piper's application to list the additional shares on the New York Stock Exchange.

The discussions were fruitful. The Piper family agreed to exchange its 501,090 shares for a package of Bangor Punta securities and Bangor Punta agreed to use its best efforts to acquire a majority of the outstanding Piper shares. Pursuant thereto, on May 8, 1969, Bangor Punta and Piper issued a release which made the usual joyful announcement of a fitting marriage, stating that the Piper family would receive Bangor Punta securities for their Piper shares and containing the following potent message:

> Bangor Punta has agreed to file a registration statement with the SEC covering a proposed exchange offer for any and all of the remaining outstanding shares of Piper Aircraft for a package of Bangor Punta Securities to be valued in the judgment of The First Boston Corporation at not less than $80 per Piper share.[3]

Chris-Craft has attacked this release and has attacked also the registration statement referred to in the release. We deal later with those issues.

Bangor Punta entered the battle with several considerable advantages. It was sponsored by the management of Piper, it could look forward to the Piper family block[4] and, significantly, it alluded to a value figure of $80, exceeding

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[3] Shortly after this release was issued, the Commission, deeming the release to be a gun-jumping offer by Bangor Punta, sought in the U. S. District Court for the District of Columbia an injunction to prohibit further similar releases before effectiveness of the Bangor Punta registration statement. Bangor Punta and Piper, without admitting any of the allegations, consented to the issuance of an injunction.

[4] One of the issues raised by Chris-Craft respecting Bangor Punta's acquisition of the Piper block relates to a guarantee by Bangor Punta to the Piper family that they would receive $80 for their stock if Bangor Punta acquired control. All parties agree that no similar guarantee inhered in the $80 value statement contained in the May 8 release.

Chris-Craft's cash tender offer and the values to be imputed to the Chris-Craft package. This was a serious blow to Chris-Craft. Accordingly, one day after Chris-Craft's exchange offer became effective, it added $10 to its package. Chris-Craft continued to acquire Piper stock until August, 1969, when it virtually ceased buying the stock. Through its succeeding exchange offers and together with its open market purchases, Chris-Craft had by then obtained 697,495 Piper shares, about 42%, while Bangor Punta, by early September, 1969, ended with slightly more than 50%. The contest for control was over except for the litigations questioning the actions of the parties along the way which has embroiled them in claims and counter-claims.

Chris-Craft's Status Under the Securities Exchange Act

Both sides have argued strenuously the question of Chris-Craft's standing to bring this action. Chris-Craft relies heavily on the language of the Court of Appeals in *Crane Co.* v. *Westinghouse Air Brake Co.*, 419 F.2d 787 (2d Cir. 1969), *cert. denied*, 400 U.S. 822 (1970), as precedent affording it status. Defendants rely on *Birnbaum* v. *Newport Steel Corp.*, 193 F.2d 461 (2d Cir.), *cert. denied*, 343 U.S. 956 (1952) and related cases for the proposition that Chris-Craft has no right to sue.

Chris-Craft's claims fall into several categories, each requiring separate consideration of the question of standing to sue.

(a) Chris-Craft made purchases of Piper stock and claims to have acted on statements of Piper about its important product lines. Even though its purchases were not from Piper, it has standing to assert such claims. *Iroquois Industries, Inc.* v. *Syracuse China Corp.*, 417 F.2d 963, 968 (2d Cir. 1969), *cert. denied*, 399 U.S. 909 (1970).

(b) Chris-Craft seeks damages from Bangor Punta claimed to have resulted from the purchase by the latter of three blocks of Piper stock, totalling 120,200 shares in May, 1969, during the pendency of their competing offers to Piper holders, in violation of SEC Rule 10b-6. Chris-Craft claims that these purchases enabled Bangor Punta to obtain majority ownership of Piper. It is held that Chris-Craft has standing to attempt to establish such a claim.

(c) Chris-Craft claims damages from the defendants on the charges that, during the pendency of Chris-Craft's attempt to take over Piper, Piper and Bangor Punta issued improper press releases and Bangor Punta filed a registration statement with material omissions and misstatements. Chris-Craft, which neither bought nor sold on the basis of the releases or registration, premises its standing to sue thereon on two grounds; one is an exception to the *Birnbaum* doctrine repeated in, *Iroquois Industries, Inc.* v. *Syracuse China Corp.*, 417 F.2d 963 (2d Cir. 1969), *cert. denied*, 399 U.S. 909 (1970); the other is predicated on a recent amendment to the Securities Exchange Act of 1934.

The first theory is that Chris-Craft is in the position of a "forced seller" as a result of Bangor Punta's acquisition of a majority of Piper's stock. Chris-Craft emphasizes the decision of the Court of Appeals in *Crane Company* v. *Westinghouse Air Brake Company*, 419 F.2d 787, 797-98 (1969), *cert. denied*, 400 U.S. 822 (1970).

In *Crane* the Court of Appeals distinguished *Iroquois Industries, Inc. supra*, (decided by the Court of Appeals five weeks prior to *Crane*—with rehearing denied by the Court of Appeals on the very day on which the *Crane* opinion was issued) by pointing out that plaintiff in *Iroquois* (a disappointed contender for control) was neither a buyer nor a seller, whereas in *Crane*, the disappointed

contender was deemed a "forced seller". Chris-Craft claims to be a locked-in buyer which could sell only at a substantial loss, and that it could not under state law (Pennsylvania) resist a merger, should Bangor Punta, as majority holder, elect to effect one.

While the "forced sale" argument here rests on quite different grounds from those expressed by the Court of Appeals in *Crane*, Chris-Craft might be within the realm of reason in asserting itself to be a forced seller, should a merger of Piper be effected under Bangor Punta's control. However, no such merger has been proposed and the "forced seller" basis for standing to sue is in this case as compared with *Crane* of highly dubious validity.[5]

The second theory on which Chris-Craft relies for standing to assert the matters relating to the press releases and registration statement is that Section 14(e) of the Securities Exchange Act affords it a right of action. Section 14(e), 15 U.S.C. §78n(e), provides:

> It shall be unlawful for any person to make any untrue statement of a material fact or omit to state any material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading, or to engage in any fraudulent, deceptive, or manipulative acts or practices, in connection with any tender offer or request

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[5] Crane Co.'s position as a forced seller was deemed to result from the fact that its target, by merging with a product competitor of Crane (Standard) made Crane an involuntary holder in its competitor and vulnerable to antitrust action. Crane thereupon sold out virtually all of the Standard holding acquired in the merger. It may be that one need not have looked beyond the merger itself to these special facts to deem Crane a forced seller. While the exchange effected in a merger has not been traditionally deemed by SEC to be a "sale" for registration purposes, it has been deemed a "sale" for purposes of invoking anti-fraud provisions.

> or invitation for tenders, or any solicitation of security holders in opposition to or in favor of any such offer, request, or invitation. *The Commission shall, for the purposes of this subsection, by rules and regulations define, and prescribe means reasonably designed to prevent, such acts and practices as are fraudulent, deceptive, or manipulative.* (Emphasis supplied).

This section was added to the '34 Act in 1968. The last sentence was added in December, 1970 (one year following the decision of the Court of Appeals, Second Circuit, in *Crane*).

In *Crane*, the Court of Appeals commented in dictum that Section 14(e) "should serve to resolve any doubts about standing in the tender offer cases, even where an offeror is not, as is *Crane*, in the position of a forced seller." 419 F.2d at 798-99. This comment may find support in *Electronic Specialty Co.* v. *International Controls Corp.*, 409 F.2d 937, 940 (2d Cir. 1969), where the target of a takeover bid, as well as that corporation's shareholders, were accorded standing to sue for alleged violations of §14(e) occurring in the course of a control fight. Judge Friendly stated that the amendment which produced section 14(e), "In effect . . . applies Rule 10b-5 both to the offeror and to the opposition" and added that "except perhaps for any bearing it may have on the issue of standing, [the amendment is] only a codification of existing case law."

The conclusions herein reached as to Chris-Craft's 10b-5 claims will be dispositive of the merits of any claim based on §14(e). Under the circumstances, the Court finds it unnecessary to decide whether §14(e) may be separately invoked by one competitor for corporate control against another.

Judge Pollack's Opinion in Chris-Craft Action

1. Piper's shareholder letter and release of January 23, 1969.

(a) One of the attacks on these communications centers on the utterance by the Piper management of its view that the $65 Chris-Craft offer was inadequate. While the offer was some $13 above the current market price, it was considerably less than a Piper holder, biding his time, could have received at later stages of the contest.

Chris-Craft insists that the communications could not be read to refer to any inadequacy of the Chris-Craft offer other than in respect to price and—to establish Piper's bad faith and intention to mislead—it points out that

(1) Piper's own bankers had advised Piper that $65 per share was a fair price and

(2) the Grumman agreement contemplated a sale of Piper stock by Piper to Grumman at $65 per share.[6]

Any Piper shareholder with a telephone or a newspaper at hand could compare the current market for Piper shares with Chris-Craft's offer. Thus, if the Piper statement of the inadequacy of the offer were intended to refer to price only it would be more fatuous than misleading. The more rational view is that the statement referred and was or should be taken to refer to other factors—such as Piper's

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[6] We do not doubt that one of the reasons for the Grumman agreement was the effect its consummation would have on the number of shares outstanding and consequently on the number Chris-Craft would have to acquire to gain control. W. T. Piper, Jr. had no hesitancy in stating that the Grumman transaction "would give us additional shares" and that it "might make the . . . tender offer of Chris-Craft less attractive to our shareholders." A psychological effect may have been intended as well—to discourage Chris-Craft early in the game by facing it with the prospect of a heavier than anticipated commitment to the contest. As noted above, the shares were never issued.

management's views as to company prospects or as to the quality of Chris-Craft management, should Chris-Craft acquire control.

That Piper's management refrained in these releases from expressing fully its personal (and in all likelihood unflattering) opinions about Chris-Craft's management does not, in our opinion, fault the communications. And if the statements were intended to convey the impression that to resist Chris-Craft Piper's management would bend its efforts to procure a better alternative for Piper shareholders, the efforts were made and were, in terms of price to tendering shareholders, successful.

Chris-Craft makes the further assertion that it was itself, as a purchaser, misled by the announcement of the Grumman agreement. Chris-Craft claims that an indication that Grumman was willing to pay $65 (in the absence of disclosure of the "put"—see n. 2 supra) helped to justify its own decision to pay that much, indicated that Chris-Craft might have a willing buyer for its block, should it decide to unload, and led Chris-Craft to refrain from exercising its right to withdraw its offer if any material increase in outstanding Piper shares were proposed or made.

While the Court has no doubt that the Grumman agreement, the announcement and their timing were strategic moves, it cannot conclude that the agreement was a sham, or that the "put" provision was anything more than what Piper purports it to be—Grumman's "out" in the event that a Grumman-Piper merger did not materialize. These were all, under the circumstances, rational steps for the Piper and Grumman managements to take and the Court cannot hold that in taking its steps Piper had any special duty to warn Chris-Craft (by disclosing the "put" or otherwise) not to gather comfort from the agreement price of $65 and not to rely on Grumman as a possible dumping ground for its shares of Piper.

Judge Pollack's Opinion in Chris-Craft Action

Chris-Craft admits that Piper described the "put" aspects of the Grumman agreement fully in its application to the New York Stock Exchange for listing of the additional shares. Chris-Craft's contention therefore that, despite its efforts to obtain a copy of the Grumman agreement, it did not learn of it until April, 1969 when two Chris-Craft representatives were elected to the Board is not worthy of belief and can evoke little more than the additional response that it could have been more sedulous than it was to protect its already heavy and growing investment in Piper.

But the fatal blow to Chris-Craft's credibility on this issue is its action after April, 1969 when it claims first to have discovered the "put" provisions of the Grumman agreement. Between April 1 and August 18, Chris-Craft acquired about 150,000 additional shares of Piper. On May 16 it added $10 to its exchange package to compete with Bangor Punta. Such behavior with knowledge of the facts is inconsistent with a claim that knowledge would have caused Chris-Craft to change its course. Plaintiff's reference to *SEC* v. *Great American Industries*, 407 F.2d 453 (2d Cir. 1968), *cert. denied*, 395 U.S. 920 (1969) (nondisclosure of finders' fees) is, under the circumstances, beside the mark.

(b) Chris-Craft has further criticized the communications for saying that Piper was in a growth industry and expected "to participate fully in this growth". The basis of its attack is in product problems faced by Piper in connection with a model then in development (Pocono) and one already on the market (Twin Comanche). These are discussed at greater length, *infra*. Here it is sufficient to point out that inherent in Chris-Craft's claim are the assumptions (1), that these problems would effectively prevent Piper from participating in the industry's growth—which it has not proved and (2), that this on-the-run re-

sponse of Piper's management to Chris-Craft's foray into the Piper stock is to be tested by the standards applicable to a registration statement—a view which this Court rejects.

Chris-Craft's contentions as to the January Piper communications and the Grumman agreement must be and are rejected as unfounded.

2. The May 8th Release

This release is one of Chris-Craft's principal targets. Chris-Craft asserts that the release was in violation of the registration and prospectus provisions of the Securities Act of 1933, especially § *5(c)* (15 U.S.C. § 77e(c)). This contention has the support of the SEC, which, in May, 1969, brought an action in the District of Columbia to restrain further releases of a similar character, with Bangor Punta consenting to a decree, and it has the support of the Court of Appeals of this Circuit, which held, in *Chris-Craft Industries, Inc.* v. *Bangor Punta Corporation*, 426 F.2d 569, 573-76 (2d Cir. 1970) that the release violated the registration requirements. The Court of Appeals nonetheless sustained the District Court's refusal to issue a preliminary injunction to prevent Bangor Punta from gaining and exercising control of Piper, but remanded the case for further proceedings.[7]

While the law of these injunction cases, as contended by Chris-Craft, may be that the May 8th release violated Sec-

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[7] Four opinions were written. Judge Waterman wrote the majority opinion for a full court (with Judge Friendly not participating). Judge Moore uttered strong doubts as to the majority's rejection of Bangor Punta's claim that the release was in conformity with SEC Rule 135, 17 C.F.R. § 230.135. Judge Anderson, who concurred in the legal conclusions of the majority, expressed separate views as to the materiality of the 8K0 statement. Judge Lumbard (then Chief Judge) could find no substance in Chris-Craft's legal claims as to Section 5(c), 15 U.S.C. § 77e(c), or Rule 10b-6, 17 C.F.R. § 240.10b-6 (to be discussed).

tion 5(c) of the Securities Act, that by no means disposes of the issue in the damage suit here being adjudicated.[8] Since Chris-Craft was not a purchaser of Bangor Punta stock it has no standing to invoke the provisions of Section 11 or 12(2) of the Securities Act of 1933 (15 U.S.C. §§ 77k, 77l(2)) (material misstatements in or omissions from registration statements) or of Section 12(1) of the Act (15 U.S.C. § 77l(1)) (sales in violation of the registration requirements). The plaintiff's claim, to be actionable in this damage suit, must rest on other grounds.

As the Court of Appeals indicated, embodying the substance of the May 8 release in a full registration statement might have served to dispel possible erroneous interpretations of the release by those to whom it was addressed and

> "... would have eliminated the possibility, perhaps the probability, that some persons would have construed the $80 figure as referring to market value when that value was neither accurate nor intended." *Chris-Craft* v. *Bangor Punta*, per Waterman, J., 426 F.2d at 575.

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[8] The issue in the "case" before the Second Circuit was whether an injunction should issue. The denial of an injunction was affirmed and it was left to the Trial Court to determine what, if any, consequences were to flow on remand from the views of the Court of Appeals as to the application of Section 5(c), 15 U.S.C. § 77e(c), of the Securities Act and Commission Rule 10b-6, 17 C.F.R. § 240.10b-6 under the Securities Exchange Act. The case before the District of Columbia Court was also one involving injunction, not damages, and Bangor Punta's consent to an order may well have been grounded on considerations other than the merits of the SEC's action. The "case" tried before this Court is radically different from the "case" considered on the appeal to the Second Circuit. Sometime after the decision on appeal, at a pre-trial hearing, Chris-Craft elected to abandon and announced the withdrawal of its claim for injunctive relief and stated that the plaintiff's sole claim was one for damages and accordingly that is the claim which is to be decided here.

Judge Pollack's Opinion in Chris-Craft Action

It must be borne in mind that this is not an action by a former Piper shareholder who exchanged his stock for Bangor Punta securities, nor is it a suit for an injunction and equitable relief.

This is a case by a disappointed contender for control attempting to invoke a registration requirement designed for the protection of the public in order to obtain damages for itself because of a premature offer to sell. Yet Chris-Craft does not point to any damage to Piper holders occasioned by the premature release, nor has it adduced any evidence that the release was anything but true when taken in its own terms—as a statement that it was Bangor Punta's intention to offer a package which would be worth $80 in First Boston's judgment.[9] Even if the release were taken as a representation of future values, it should be noted that actual values reached by the Bangor Punta package were so close to $80 as to render any variance *de minimis*.[10]

Any claim of Chris-Craft that the violation of Section 5 *per se* induced enough Piper holders to accept Bangor Punta's offer to tip the balance of control in Bangor Punta's favor must be supported with proof that this re-

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[9] The Court is familiar with instances in which exchange offers contemplate, and describe, formulas guaranteeing a market value for the securities to be given in exchange for the target company's stock. Such descriptions are common and leave no doubt as to their intentions. The language of the May 8 release could not be confused by reasonable men (much less professionals of the purported stature of Chris-Craft's witness on the point) with offers intending or implying guarantees of market value.

[10] Based on various alternative methods of valuing the Bangor Punta package in the week following July 23, five days after effectiveness of the Bangor Punta exchange offer, the Bangor Punta package had a high market value of $79.93 and a low of $73.37. By contrast, using the same bases, Chris-Craft's package in the period had a high of $75.50 and a low of $63.25.

sulted from the absence of the information which a full registration statement and prospectus would have contained. Chris-Craft has made no such showing. Moreover, a showing that the acquisition of a particular block was enough to give Bangor Punta control would not by itself constitute proof that control would have fallen to Chris-Craft if Bangor Punta had failed to acquire that particular block. While the delay which might have occurred in the processing of a full registration statement by Bangor Punta might have given Chris-Craft extra time to forage about for Piper stock while Bangor Punta was preparing its statement for filing, Chris-Craft has adduced no proof that it was disadvantaged in this regard. *Cf.* 426 F.2d at 573.[11]

Chris-Craft did respond to the May 8 release by raising its bid. Its cost of acquiring Piper stock was thereby directly and immediately increased. But everything in this record is consistent with the conclusion that Chris-Craft would have done the same thing even if the substance of the release had been embodied in a fully cleared prospectus. There is nothing in this record which shows that the release was, in intent or effect, false or misleading as to Chris-Craft or the public.[12] Any increase in Chris-Craft's costs occasioned by the release was occasioned by its substance and not by the absence of a registration statement.

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[11] "We do not understand Chris-Craft to allege that prior misdeeds of Bangor Punta so determined the course of the competition for shares after the date of the decision below that Chris-Craft was placed at any real disadvantage."

[12] It must be borne in mind that the fact that a statement violates Section 5 of the Securities Act, 15 U.S.C. § 77e, does not necessarily connote that the statement is either false or otherwise misleading within the meaning of Rule 10b-5 upon which Chris-Craft relies. A thoroughly adequate disclosure—even a full registration statement—used in offers to sell before a required filing violates Section 5.

Chris-Craft fully understood what the release was meant to convey. Chris-Craft is not entitled in this suit to the recovery of damages under Rule 10b-5 for the violation of Section 5.

3. The Bangor Punta Registration Statement[13]

Chris-Craft complains of the Bangor Punta registration statement covering the package of securities it was offering in exchange for Piper stock, alleging that material falsity in the statement was part of the scheme to divert Piper holders away from Chris-Craft.

The principal attack is on the figure at which Bangor Punta carried its holdings (almost 100%) of the Bangor and Aroostook Railroad (BAR). Bangor Punta carried the BAR stock on its books at $18.4 million—an [illegible] tional figure in terms of transactional accounting [illegible] with a checkered history.

Historical cost of the BAR stock, less depreciation and other accounting adjustments, was $29.8 million. In 1965, in view of a then possible sale of BAR, Bangor Punta wrote the asset down to some $8 million. That sale did not materialize and the carrying figure was again revised (this time upward) to reflect an $18.4 million valuation of its BAR investment by investment bankers. The book increase resulting from this revaluation was credited directly to earned surplus (bypassing the income accounts).

There is no dispute as to this series of adjustments. The $18.4 million carrying figure is, however, attacked as materially misleading in view of a sale of Bangor Punta's

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[13] A fuller discussion of this issue is contained in this Court's opinion in *SEC* v. *Bangor Punta, et al.*, 331 F. Supp. 1154 (S.D. N.Y. 1971) (Pollock, *J.*). Only high-light facts are here discussed.

interest in BAR, at $5 million (and additional contingent consideration) which did occur in October, 1969, a few months following effectiveness of Bangor Punta's registration of its Piper exchange package.

Chris-Craft asserts that the agreement to sell the road at that figure existed earlier and should have been reflected in Bangor Punta's registration statement. The charge is that Bangor Punta postponed formal contract and closing to avoid having to reflect in its registration statement a book loss of $13 million on the sale.

In *SEC* v. *Bangor Punta*, n. 13 *supra*, this Court concluded that there was no substance in similar allegations by the SEC regarding the BAR matter. We held, however, that the registration statement was unintentionally in error in failing to disclose the circumstances which rendered Bangor Punta's carrying figure of the BAR holding obsolete and misleading absent such disclosure. An injunction against further violation of the securities laws was sought by SEC in that case but was denied. However, the Court ordered that shareholders who accepted the Bangor Punta exchange offer be given an opportunity to rescind their exchange should they elect to do so because of the registration error. This result expressed the principle that a registration statement with a misleading effect should be corrected for those to whom it related, whether or not the error was made with intent to mislead.

But that result does not conclude the issue here. This is not a suit by a Piper shareholder claiming to have been damaged by the error in respect to the BAR or any other matter pertaining to the registration. Chris-Craft did not rely on or purchase under the registration statement filed in connection with the exchange of Piper shares for Bangor Punta securities and, for the following reasons, we cannot

conclude that plaintiff merits, under the circumstances, any recovery under federal law on this branch of the case.

Chris-Craft's complaint with respect to the Bangor-Punta statement is not based on the provisions of the Securities Act expressly designed for such complaints. Secs. 11 and 12, 15 U.S.C. §§ 77k and 77*l*. It does invoke the broad provisions of Section 10, 15 U.S.C. § 78j and Rule 10b-5, 17 C.F.R. § 240.10b-5, under the Exchange Act, and of Section 14(e), 15 U.S.C. § 78(n)(e), under that Act. It thus presents us with the question whether and to what extent these general provisions can fairly be construed to override the more specific ones prescribed to implement private actions in complaint of registration statements.

We have no doubt that a violation of the registration requirements can, also, be a violation of Section 10b(5) and 14(e) of the Securities Exchange Act. But the mere fact of a violation of registration requirements under the '33 Act does not automatically trigger Section 10b and Rule 10b-5. The reasons and basis for invoking the '34 Act provisions must exist independently. The essentials are material deception, some form of scienter and a causal relation between the deficiency and the harm complained of. These essential elements have not been established in this case. At a minimum, neither a form of scienter nor proof of causal effect was established here.

Chris-Craft does not, in this Court's view, stand in the position of the plaintiff in *Mills* v. *Electric Autolite*, 396 U.S. 375 (1970) as being entitled to ask the Court to disregard traditional requirements that a causal connection be shown between the claimed violation and the injury. The attack in *Mills* was on a proxy statement which did not adequately disclose the true interest of directors who recommended a merger. This omission directly affected the shareholders on whose behalf the suit in *Mills* was

brought.[14] It was in that particular context that the Supreme Court deemed sufficient a set of facts under which shareholders *could* be misled.[15] This does not aid Chris-Craft as it is seeking to recover because of the effect which a misstatement allegedly had on third parties.

A Piper holder's decision to tender to Bangor Punta and Chris-Craft's failure to acquire the shares of such a holder cannot be held to be so clearly tied to the registration statement as to obviate the need for proof which would, at least, indicate a causal connection producing damage to Chris-Craft.

Chris-Craft was indeed a Piper shareholder. But it did not exchange any of its Piper shares for Bangor Punta. Its complaint is solely that of a defeated contender for control and it has asked this Court for a money award in the absence of evidence establishing a reasonable probability that its defeat and damage were connected with the claimed violations. There is no proof that a single exchanging Piper shareholder would have refrained from the exchange *and* taken an offer for his shares from Chris-Craft instead of that from Bangor Punta. In a damage suit, as distinct from one for equitable relief, such proof is essential to sustain a 10b-5 claim. In effect, Chris-Craft seeks the windfall of a punitive award against Bangor Punta by assuming the role of defender of the public

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[14] See *J. I. Case Co.* v. *Borak*, 377 U.S. 426, 428 (1964), ("We consider only . . . whether § 27 of the Act authorizes a federal cause of action . . . to a *corporate stockholder* [arising from use of a misleading proxy statement]" (emphasis added)).

[15] "Where there has been a finding of materiality, a shareholder has made a sufficient showing of causal relationship between the violation and the injury for which he seeks redress if, as here, he proves that the proxy solicitation itself, rather than the particular defect in the solicitation materials, was an essential link in the accomplishment of the transaction." *Mills*, 396 U.S. at 385.

interest in the purity of the registration process. This role has already been assumed by the Commission and we could well expect it to be assumed by exchanging Piper holders if there were material harm to them.

Both *Crane* and *Mills*, *supra*, indicate that in a proper case "tendency to result" may be as good coin as "result" and "could" be as good as "did" in establishing a right of action. The evidence does not support a notion that the Bangor Punta registration statement presents such a case. Despite the language of *Crane*, the facts indicated that blatant manipulation (overt buying and covert selling) was used to "paint the tape" as Court of Appeals Judge Smith said. By this means a competitor for control (Standard) was able, on the crucial days of Crane's tender offer, to raise the price of target company (Westinghouse Air Brake) stock to a level which assured defeat of Crane's campaign. The character of the violation and the clear causal nexus were crucial to the *Crane* result. These characteristics have not been demonstrated here. In *Mills*, as pointed out *supra*, the suit was on behalf of and for protection of the class to which the proxy material was addressed and for which the proxy rules were designed.

Granting to Chris-Craft full standing to raise the issue of falsity in the Bangor Punta registration statement would, in this Court's view, permit it to do no more than it has done here—attempt to show what it has not been able to show, that as a matter of substance the claimed violations entitled it to money damages.

Nor does Section 14(e) in any way alter the result on the merits. Accepting, on its face, the dictum of the Court of Appeals in *Crane* that Section 14(e) "should serve to resolve any doubts about standing in the tender offer case, even where an offeror is not, as is *Crane*, in the position of a forced seller", 419 F.2d at 798, leaves open the ques-

tions of how the substantive standards of Section 14(e) are to be applied and what levels of proof are required to evoke their application.

Section 14(e) virtually tracks the language of Rule 10b-5, with certain notable exceptions, and our 10b-5 conclusions are dispositive of the issues as raised under Section 14(e). The differences in language are significant. Section 14(e) refers to "fraudulent or manipulative acts or practices" whereas Rule 10b-5 makes unlawful "any act, practice or course of business which operates *or would operate* as a fraud or deceit on any person" Rule 10b-5(c) (italics added), and contains a prohibition against employment of "any device, scheme or artifice to defraud", Rule 10b-5(a) (language not present in Section 14(e)). In the context of the facts of this case, Section 14(e) adds no weight to contentions of Chris-Craft that it need not establish a nexus between the violations it charges and the damages it claims to have suffered.

In addition to the charge of deficiency in the registration statement based on the BAR carrying figure, Chris-Craft has alleged the failure of the statement to reflect the terms of outstanding institutional loans, the relatively favorable treatment to members of the Piper family in the exchange (see n. 4 *supra*) and a guaranty to a group of Piper holders (the "Bolles" group), ostensibly for tax purposes, of a resale price for the Bangor Punta package of not less than 32½% of the value thereof at the close of the exchange. The Bangor Punta prospectus, while it did not pinpoint each of the alleged deficiencies made it more than amply clear that special treatment was being afforded by Bangor Punta to management personnel of Piper—so that the willingness of these large holders to effect the exchange for Bangor Punta may have been conditioned by their personal advantages as well as their views as to the best

interests of Piper. Thus Chris-Craft's charges, in essence that this motivation was not disclosed, resolve themselves into a dispute over adjectives. None of the registration errors, including the BAR item, went beyond mere negligent omission of misstatement of fact.

4. Application of Rule 10b-6

SEC Rule 10b-6 interdicts bids for or purchases of a security by or on behalf of the issuer of a security if the security is "the subject of . . . [a] distribution". Included in the prohibitions are bids for or purchases of "any right to purchase any such security."[16]

Bangor Punta made three block purchases of Piper shares during the pendency of its exchange offer. It purchased 78,600 shares from Fund of Funds Proprietary Fund, Ltd. (Proprietary) and two blocks, totalling 41,600 shares, from Bay Securities Corporation and American Securities. Chris-Craft claims that all three blocks were purchased in violation of the Rule. Bangor Punta claims the benefit of an exemption from the operation of the Rule for the purchase from Proprietary. Rule 10b-6(a)(3)(2), 17 C.F.R. 240.10b-6(a)(3)(ii)(1971).

The application of the prohibitory provisions of Rule 10b-6 is not before us for *de novo* decision. The Court of Appeals has ruled that Bangor Punta's purchases violated the first sentence of the Rule. However, it left open two vital questions to be decided on the remand. One is whether the exemption contained in paragraph (a)(3)(2) of Rule 10b-6 is applicable. The other is the determination of what remedy is appropriate.

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[16] There is no dispute that, under the circumstances of this case, Piper stock was, within the meaning of the Rules, a "right to purchase" Bangor Punta stock.

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Paragraph (a)(3)(2) of Rule 10b-6 exempts

> unsolicited privately negotiated purchases, each involving a substantial amount of such security [in distribution], effected neither on a securities exchange nor from or through a broker or dealer.

As stated above, Bangor Punta claims an exemption from Rule 10b-6 only for the Proprietary block. A literal reading of the exemption requires a finding that the Proprietary purchase, like the others, was not exempted.

Proprietary's functions appear to have been solely to execute transactions for its associated mutual funds.

The Proprietary purchase followed a visit by a Bangor Punta executive with officials of Proprietary in Nassau, and it appears further that Bangor Punta made a payment of 75c per share to London & Dominion Trust Company, Ltd., which acted as nominee for Proprietary's Piper holding.[17] Absent any other cogent explanation for the visit the facts seem to point fairly at a solicitation of the purchase from Proprietary as the reason for the visit. It is so found.

The Court has searched for substance in the 10b-6 contention behind the technical violation, in the context of a claim for damages rather than in a suit for injunction.[18]

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[17] Chris-Craft claims that this was a commission payment. Bangor Punta asserts that it was a fee. Resolution of this issue is unnecessary. Commission payments are not prohibited by the exemption (except by implication from the exclusion of purchases through a broker). The status of the seller as a broker-dealer as well as the "solicitation" involved in the Nassau visit are in themselves enough to deprive the transaction of an exemption under a literal reading of paragraph (a)(3)(2) of Rule 10b-6.

[18] It has been suggested in some quarters that Rule 10b-6 is of doubtful application in cases such as the one at bar. The stock bought by Bangor Punta was Piper stock, not its own. Since it was

This search has not revealed such substance as to merit serious consideration of the charge as a basis for money damages.

Despite the failure of Bangor Punta's acts to match the literal prescriptions of the exemption, this Court cannot conclude that Chris-Craft has established any right to recovery under Rule 10b-6. Even granting that the block purchases resulted arithmetically in Bangor Punta's achievement of control, there is no basis for concluding that, absent Bangor Punta's acquisition of these blocks, Chris-Craft would have achieved its goal of control. Thus the record will not support a contention that Bangor Punta should, by reason of violation of Rule 10b-6, compensate Chris-Craft for the latter's failure to gain control of Piper.

1. Chris-Craft was not misled by the purchases of Piper stock effected by Bangor Punta during the "distribution" of Bangor Punta's stock in the Piper exchange. The primary purpose of Rule 10b-6 is to prevent bids or purchases

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embarked on a program of purchasing Piper and its self-interest would cause it to seek to do so as economically as possible, it would have no reason to stimulate demand by others for or inflate the price of Piper stock. Its motivation would, therefore, be to adhere to rather than violate the purpose of Rule 10b-6. While Piper stock and not Bangor Punta stock was being purchased, the purchases fell within the Rule because Piper stock was exchangeable for the stock being distributed—i.e., Bangor Punta stock. Any rise in Piper would in effect depress the value of Bangor Punta securities offered in exchange. But even if the price of Bangor Punta's securities were somehow being stimulated that rise would be of no avail to Bangor Punta in the exchange. For market arbitrage would almost immediately raise the price of Piper to align it with the rising price of the Bangor Punta securities offered in exchange.

These considerations, however, are foreclosed to this Court by the Court of Appeals which has found Rule 10b-6 to be violated and which remanded solely to have determined the question of the exemption and the appropriate remedy, if any, in the context of a suit demanding an injunction (which this no longer is).

by a distributor of securities which have a stimulating effect on the market. The Rule thus seeks to protect a potential buyer from paying a price for the security in distribution other than that set by untrammeled market demand or from being misled into believing that the market demand is wholly that of independent purchases. See *SEC* v. *Scott Taylor and Co.*, 183 F. Supp. 904, 907 (S.D. N.Y. 1959). Chris-Craft was not in that position. It knew that significant large blocks of Piper stock were in existence, that Bangor Punta was as anxious as Chris-Craft to acquire those blocks and that Bangor Punta's acquisitions (like its own) would place such blocks at a premium.

2. Was the public misled by Bangor Punta's acts? Here too there is not a scintilla of evidence that any Piper holder was misled. And the absence of such evidence may be explained by the fact that the acts of Bangor Punta here in question, while they did not comply with the literal terms of the exemption contained in paragraph (a)(3)(2) of Rule 10b-6, were nevertheless well within the spirit of that exemption. This is a root factor in determining whether the 10b-6 charge has real substance. For the exemption from the prohibitions of the Rule, in a vital sense, defines the basic purposes of the Rule by delineating the kinds of transactions which have little, if any, tendency to radiate a stimulating effect into the general market.

If we lay the transactions complained of against the intent behind the words of the exemption provisions it becomes clear that the block purchases fell within the intent of the exemption, if not within its words.

(i). Paragraph (a)(3)(2) requires that purchases, to be exempt, must be substantial. The obvious reason for this provision is to prevent fragmenting purchases in order to create the appearance of a spread of demand. There is

no dispute that Bangor Punta's block purchases were of a substantial nature. There is no evidence that Bangor Punta fragmented its purchases or otherwise acted to produce or heighten a stimulating effect on the market.

(ii). A distributor's solicitation of purchases, while distribution is in process, may have the same effect as purchases by the distributor. It may create an appearance of demand which is artificial in fact. However, while we have concluded that the visit of a Bangor Punta executive to Nassau was to solicit a sale to Bangor Punta by Proprietary, it was not solicitation calculated to have the effect condemned by the Rule. There is no evidence that it was broadcast, or that it was otherwise radiated into the general market where it might have had the prohibited stimulative effect. And, even if the payment of 75¢ per share to Proprietary's nominee bank were deemed to be part of the inducement to acquire the block, that fact does not change the local and unpublicized character of the entire Proprietary transaction.

(iii). A purchase on an exchange cannot be exempted. The reason is obvious—and casts a consistent light on the prime purpose of the Rule; a purchase on an exchange becomes a broadcast item and consequently one of the components of the price trend of the security. The purchases complained of were not effected on an exchange.

(iv). Purchases from or through brokers or dealers cannot, technically, be exempted. This element of the exemption has the same function as the requirement that the purchase not be made on an exchange. Brokers and dealers are constantly quoting, broadcasting and varying their quotes with indications of change in supply and demand. Thus a purchase from or through a broker or dealer, even though in the over-the-counter market, may have the same tendency to affect market price. But neither Proprietary

(from which 78,600 Piper shares were purchased) nor Bay Securities Corporation (from which blocks aggregating to 21,600 Piper shares were purchased) was a broker or dealer in the conventional sense. Both were "in-house" facilities of mutual fund complexes acting for the funds they served. As such they may well have had the policy of secrecy which characterizes the operations of many funds during the period of acquisition or disposition of blocks. It is a common mutual fund practice to report even significant trades under a "miscellaneous" and unidentified rubric until the intended amount to be purchased or sold has been reached—and then often only in periodic reports after the fact and merely as a change buried in a list of one hundred or more portfolio holdings.[19]

5. *Piper Product Problems*

We deal here with the complaint of Chris-Craft that, as a purchaser of Piper securities, it relied to its detriment on statements of Piper rendered materially false and misleading because of certain vital omissions.

Piper, in its 1967 and 1968 annual reports and in certain other public statements, had issued optimistic reports about a new development (the Pocono plane) and about a principal product (the Twin Comanche) the latter accounting for a significant portion of its revenues. In fact, both of these products were facing serious problems. The Pocono depended for its successful development on an engine to be created by Aveo Lycoming. Lycoming, despite its attempts to create one with the required horsepower, failed

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[19] Some time after the occurrence of the events litigated in this case the SEC adopted Rule 10b-13. That Rule interdicts (with exceptions not here pertinent) any purchase by a tender or exchange offeror otherwise than through the tender or exchange. It is a *post hoc* regulation which cannot be applied here.

to do so. The Pocono project, whose continuation or abandonment was a subject of dispute within Piper, was in fact abandoned by Bangor Punta shortly after it acquired control.

The Twin Comanche, while it was extensively sold and used, had operating characteristics which required especial skill and alertness of the pilot for safe handling. At some time or other various governmental agencies had noted and commented on these characteristics and between its inception in 1962 and May of 1969 the Twin Comanche had been involved in 62 fatal accidents resulting in over 130 deaths. Of the 62 accidents, 29 were the result of stall-spins —a propensity of the plane apparent from prior tests.

Chris-Craft complains of a 1967 annual report which described the Pocono as Piper's "major advanced research project", that indicated that the plane was undergoing flight tests, that deliveries of the plane were expected to begin in 1970 and that plans were in progress to build a plant in Florida for manufacture of the product.

The specific criticism levelled against this report by Chris-Craft is as follows:

> Nowhere was the public cautioned that the plane being tested had only an interim engine, that Avco Lycoming had not yet delivered or manufactured the engine required for the plane, and that the success of the venture hinged entirely on the ability of Lycoming to produce an engine powerful enough for the Pocono to meet FAA certification requirements or that it had encountered difficulties and delays in doing so.

Piper, on its side, points to statements in its reports and in trade articles which it claims put the Pocono project in its proper perspective as an "experimental project" "being

tested". It asserts that at no time until September, 1969, was there a discussion of abandoning the project, let alone a decision to do so. Piper points out also that as late as August, 1969, Lycoming said that it could produce, promptly, the required engine for the Pocono. And the testimony of Bangor Punta's chief executive indicates that cost (as well as engineering) was a significant factor in his decision to abandon the project. There is every indication that if the Pipers had remained in control, the Pocono would not have been abandoned.

We cannot find that Piper's statements, even when viewed in the light of subsequent difficulties and eventual abandonment of the Pocono project, could be deemed materially false as of the time they were made. Chris-Craft denies that it is exercising "hindsight". However, the problems it points to, viewed as of the time of Piper's statements, seem little different from those attending many eventually successful product developments. While it is not easy, in considering the Twin Comanche, to avoid interlacing into the issues of this case the general public policy of air safety, that must, in this Court's view, be done. Chris-Craft has not shown that adjusting the Twin Comanche would be so costly or that limiting the plane to use by experienced pilots would so seriously damage Piper's future as to require it to damage itself by the disclosures claimed necessary to avoid the charge of fraud.

The evidence is convincing that Chris-Craft's original decision to acquire Piper was made without knowledge of the Pocono and Twin Comanche problems—and avowedly with knowledge of little more than what was carried in standard reference sources available in brokerage offices. Despite the fact that by April, 1969 Chris-Craft had two representatives on the board of Piper it did not, it claims, learn of the Pocono and Twin Comanche problems until

September of 1969. By then, its purchasing was over and Bangor Punta was in control.

However, the record affords considerable support for the conclusion that Chris-Craft went into its stock purchasing with no concern about these product problems. The record fairly requires the inference that incidents involving the Twin Comanche and official reports on its operating characteristics could have been timely learned and timely appraised by anyone wishing and able to commit millions to a campaign for control of Piper. The claimed lack of knowledge or notice of products problems is not credi-

Chris-Craft asserts that it relied on Piper's statements (claimed to be misleading because of omissions) respecting the Pocono and Twin Comanche is making its heavy investment in Piper. However, Chris-Craft has not convinced the Court that these products, or what Piper said of them, were considered or material in Chris-Craft's investment decision. To demonstrate the materiality of the Pocono development, Chris-Craft asserts:

> Technology Fund, a mutual fund with no greater expertise about the aircraft industry than Chris-Craft, was Piper's largest record shareholder outside of the Piper family as of January 1969. . . . A Technology Fund research report dated November 19, 1968—more than a month before Chris-Craft's first purchase of Piper—stated, in part:
>
> At 52 Piper is adequately priced and little appreciation is expected until the anticipated extremely favorable third quarter. Quite possibly Piper could go to 18 times 1969 earnings, which produces a price of 63. However, at that level, it would be fully priced and sale would be in order except that before sale, the Pocono's outlook should be reviewed, as it really dominates Piper's future.

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The demonstration shows more than it was intended to. As matters stood when the Technology Fund report was written, the Fund was not misled by Piper's reports. It appraised Piper as "adequately priced" at 52. A price of 63 would justify a sale unless a later review of the Pocono development might indicate otherwise.

Chris-Craft, within weeks after this report by the experts of the Fund, paid the Fund more than $6,500,000 to acquire some 101,000 Piper shares held by the Fund. With no more (and perhaps less) information *at the time* than was then available to the Fund's experts it over-anticipated the Fund's most bullish possibility of market value ($63) based on earnings reports and bought deep into the future of Piper and, it claims, Pocono. The "materiality" of the Pocono development is amply demonstrated by this Fund report, but, significantly, materiality as a possibility to be closely watched, not one to be blindly bought. Chris-Craft did not rely on Piper's statements in this regard.

In balancing equities in suit by an ordinary investor this Court might weigh differently the competing duties of Piper's management: on the one hand, to avoid damaging the company by airing internal problems (which with respect to Pocono did not at the time foreshadow the ultimate abandonment of the project and, with respect to Twin Comanche, were not as irremediable as Chris-Craft wishes us to believe) and on the other hand, to avoid a misleading effect in its published statements. But Chris-Craft, under the circumstances of this case, does not merit a weighing in its favor of so delicate a set of duties. In effect, Chris-Craft's management is attempting on this issue to enlist the Court's aid in passing over to others the burden of a purported harm to Chris-Craft's shareholders which Chris-Craft's management could well have avoided by reasonable inquiry. The credible evidence adduced in Chris-Craft's favor does not warrant such a result.

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The Claim against First Boston

First Boston and Paul L. Miller and Nicholas H. Bayard of First Boston (the "First Boston defendants") were joined as parties defendant herein. On the basis of the record, the Court cannot find that they committed, or engaged in any course of conduct which operated as fraud or deceit upon Chris-Craft or the public shareholders of Piper.

Indeed, were the record to support Chris-Craft's claims with respect to Piper and Bangor Punta (which it does not) the Court would be hard put to find any basis for extending liability to the First Boston defendants.

First Boston, in its capacity as an investment banker, rendered a variety of professional services to Piper Aircraft Corporation, Bangor Punta and members of the Piper family. In each case, substantive decision making power rested with and was exercised by these clients and not First Boston. First Boston was not responsible for the Piper letter to shareholders dated January 27, 1969. There is no evidence that it did more than contribute to the letter a suggestion within its area of expertise (investment prospects in the light aircraft industries generally), of which plaintiff does not complain.

The suggestions to Piper made by the First Boston defendants in respect to: the cash tender offer by Chris-Craft, the Grumman agreement, the press release concerning Grumman, the U.S. Concrete and Southply transactions, the May 8, 1969 agreement between Bangor Punta and the Piper family, the May 8, 1969 press release in connection therewith, the purchases by Bangor Punta of large blocks of Piper and the prospectuses on the Piper exchange offer, were a legitimate exercise of and limited to professional advice within the area of expertise of First Boston.

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The activity of First Boston in the course of its professional relations with Piper, the Piper family and Bangor Punta does not render it responsible or liable for the actions of its clients. The record compels the conclusion that the First Boston defendants acted solely in the furtherance of what they believed in good faith to be the legitimate interests of their clients.

The Relief Requested

The Court of Appeals, with all Judges concurring, affirmed Judge Tenney's denial of a preliminary injunction and the case was remanded to the District Court for further proceedings not inconsistent with the majority's opinion. However, at a pre-trial conference, the plaintiff announced its election on the record to have its case considered as only a straight non-jury damage case rather than an equitable suit for injunction. No such case had been tendered to the Court of Appeals for consideration and the merit of Chris-Craft's suit in support of a damage claim was not before the Court of Appeals.

Chris-Craft acknowledges that its original attempt to have Bangor Punta divested of its majority control was a quest beset with inherent practical difficulty[20] and it gives this as the reason for now seeking damages only. In view of the conclusions reached by the Court on the issues raised by Chris-Craft, it is not necessary to pass on Chris-Craft's theory of computing the damages. However, an analysis of the damage issue here raised will illustrate the anomalous consequences which may flow from according status to sue to disappointed contenders for control,

[20] Among other things. Chris-Craft asserts that changes effected in Piper under Bangor Punta control render Piper a different company from that into which Chris-Craft bought.

even in cases with more substance and merit than are present in the case at bar.

Chris-Craft evaluates its damages in terms of the appraisal value of its Piper stock in the light of the ability of Bangor Punta to compel a merger at any time. Recognizing the wide disparity of opinion in respect to such value on the part of "experts", Chris-Craft suggests the possible use of the procedure used elsewhere, [21] permitting an aggrieved plaintiff to tender its shares to defendant at cost.

The proximate victims of virtually all the alleged violations of which Chris-Craft complains are one-time Piper stockholders who now hold Bangor Punta stock. These are the very people against whom Chris-Craft wishes us (by a judgment against their company) to assess many millions of dollars of damages in the form of a bail-out of Chris-Craft from its misadventure in Piper.

Were every allegation of Chris-Craft supported by the record, neither reason nor justice would permit such a result. Insofar as the Piper corporation is concerned, the results of assessing damages against it would be equally anomalous. It was the prize in the battle, not a contender. Its equity is held by three distinct groups: Bangor Punta, Chris-Craft, and a small public minority which did not tender shares in the various exchanges proffered. We have already pointed to the reasons for excluding Bangor Punta from the pale of liability. Chris-Craft, of course, would be bailed out if its theory of damages were accepted. This leaves the non-exchanging Piper holders. This is the category of holders intended to be protected. There is no stretch of reason or justice which could conceivably draw

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[21] *Gottlieb* v. *Sandia Amer. Corp.*, 304 F. Supp. 980 (E.D. Pa. 1969).

them indirectly into the circle of liability. See, *SEC* v. *Texas Gulf Sulphur Co.*, 401 F.2d 833, at 867 (2d Cir. 1968), *cert. denied*, 394 U.S. 976 (1969), *sub nom., Coates* v. *SEC*, *Kline* v. *SEC*.

However, even properly chosen defendants must be shown to be more than putatively liable. That has not been done with respect to any defendant named by Chris-Craft herein.

While the details of every issue and argument in Chris-Craft's case have not been discussed herein, they have been considered and have not been found to warrant a judgment for Chris-Craft against any of the defendants.

The complaint against the corporate defendants, Bangor Punta and Piper, is dismissed and on the basis of the findings and conclusions herein expressed, the complaint is *a fortiori* dismissed as to all personal defendants.[22]

Counterclaim of Piper Aircraft

Piper has asserted a counterclaim against Chris-Craft charging that the latter violated Sections 13(d) and 14(e) (as well as 10b) of the Exchange Act.[23] This counterclaim repeats virtually all of the contentions made by the plaintiff in *Bangor Punta* v. *Chris-Craft*, S.D.N.Y. 69 Civ. 2354, which is being decided this day. Piper asks this Court to "fashion an appropriate equitable decree to deprive Chris-Craft of the benefit of its violation."

Piper was the unwilling target of Chris-Craft's bid for control of Piper. To avert what it deemed to be a raid by

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[22] The agreed findings stipulated by the parties as such are found even if not fully covered herein, *non constat* many are evidentiary rather than findings of ultimate fact.

[23] § 13(d), 15 U.S.C. § 78m(d) (1971); § 14(e), 15 U.S.C. § 78n(e) (1971); § 10(b), 15 U.S.C. § 78j(b) (1971).

Chris-Craft, it invited Bangor Punta to compete with Chris-Craft. Bangor Punta acceded and (with the aid of the substantial blocks of Piper stock held by the Piper family and other significant cooperation of Piper's management) it won the contest. While both contestants may, today, be less than happy at the outcome, Piper was the prize, not a contender. The Court is at a loss to envisage any form of equitable (or other) relief to which Piper might in reason and justice be entitled. Piper's case against Chris-Craft, like Bangor Punta's rests shakily on surmise and speculation and much of it, even if sustainable, is irrelevant to any damage which Piper does or could claim.

The counterclaim of Piper against Chris-Craft is dismissed for failure to sustain the burden of proof thereof.

The foregoing shall constitute the findings and conclusions required by F. R. Civ. P. 52(a).

So Ordered.

December 10, 1971

Milton Pollack
U. S. District Judge

APPENDIX H

Opinion of the Second Circuit Court of Appeals in *Chris-Craft Industries, Inc.* v. *Piper Aircraft Corporation et al.*; *Bangor Punta Corporation* v. *Chris-Craft Industries, Inc.*; and *Securities and Exchange Commission* v. *Bangor Punta Corporation*, dated March 16, 1973.

March 16, 1973, Second Circuit Opinion

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

Nos. 805-08—September Term, 1971.

(Argued August 14, 1972 Decided March 16, 1973.)

Docket Nos. 72-1053, 72-1064, 72-1120, 72-1140

DOCKET NO. 72-1064

CHRIS-CRAFT INDUSTRIES, INC.,

Plaintiff-Appellant,

v.

PIPER AIRCRAFT CORPORATION, HOWARD PIPER, THOMAS F. PIPER, WILLIAM T. PIPER, JR., BANGOR PUNTA CORPORATION, NICOLAS M. SALGO, DAVID W. WALLACE, THE FIRST BOSTON CORPORATION, PAUL L. MILLER and NICHOLAS H. BAYARD,

Defendants-Appellees.

DOCKET NO. 72-1120

BANGOR PUNTA CORPORATION,

Plaintiff-Appellant,

v.

CHRIS-CRAFT INDUSTRIES, INC.,

Defendant-Appellee.

March 16, 1973, Second Circuit Opinion

DOCKET NOS. 72-1053 and 72-1140

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff-Appellant-Appellee,

v.

BANGOR PUNTA CORPORATION,

Defendant-Appellee-Appellant.

Before:

MANSFIELD and TIMBERS, *Circuit Judges,* and GURFEIN, *District Judge.**

Appeals from judgments entered after non-jury trials of three separate but related civil actions in the Southern District of New York, Milton Pollack, *District Judge,* involving alleged violations of the antifraud provisions of the federal securities laws in connection with the contest between Chris-Craft Industries, Inc. and Bangor Punta Corporation for control of Piper Aircraft Corporation.

Affirmed in part; reversed and remanded in part.

ARTHUR L. LIMAN, New York, N.Y. (Stuart Robinowitz, Joseph J. Ackell, Jack C. Auspitz, Anthony M. Radice and Paul, Weiss, Rifkind, Wharton & Garrison, New York, N.Y., on the brief), *for Chris-Craft Industries, Inc. (Plaintiff-Appellant in No. 72-1064; Defendant-Appellee in No. 72-1120).*

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* Of the United States District Court for the Southern District of New York, sitting by designation.

ZACHARY SHIMER, New York, N.Y. (Paul G. Pennoyer, Jr., Irene C. Warshauer and Chadbourne, Parke, Whiteside & Wolff, New York, N.Y., on the brief), *for Piper Aircraft Corporation, Howard Piper, Thomas F. Piper and William T. Piper, Jr. (Defendants-Appellees in No. 72-1064).*

JAMES V. RYAN, New York, N.Y. (William L. D. Barrett, C. Kenneth Shank, Jr. and Webster Sheffield Fleischmann Hitchcock & Brookfield, New York, N.Y., on the brief), *for Bangor Punta Corporation (Defendant-Appellee in No. 72-1604; Plaintiff-Appellant in No. 72-1120; Defendant-Appellee-Appellant in Nos. 72-1053 and 72-1140) and for Nicolas M. Salgo and David W. Wallace (Defendant-Appellees in No. 72-1064).*

JOHN F. ARNING, New York, N.Y. (Roger L. Waldman, Charles W. Sullivan, and Sullivan & Cromwell, New York, N.Y., on the brief), *for The First Boston Corporation, Paul L. Miller and Nicholas H. Bayard (Defendants-Appellees in No. 72-1064).*

ROBERT E. KUSHNER, Assistant General Counsel, SEC, Washington, D.C. (G. Bradford Cook, General Counsel, David Ferber, Solicitor, and James J. Sexton, Attorney, SEC, Washington, D.C., on the brief), *for Securities and Exchange Commission (amicus curiae in No. 72-1064; Plaintiff-Appellant-Appellee in Nos. 72-1053 and 72-1104).*

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March 16, 1973. Second Circuit Opinion

TIMBERS, *Circuit Judge:*

PRELIMINARY STATEMENT

These consolidated appeals present important questions, some of first impression, involving the antifraud provisions of the federal securities laws in their application to a contest for acquisition of a controlling stock interest in a target corporation. Among the questions presented are those involving the scope of liability and relief under Section 14(e) of the Securities Exchange Act of 1934 and the type of relief necessary, in an SEC enforcement proceeding, to effectuate the broad remedial purposes of the federal securities laws.

The appeals are from judgments entered after non-jury trials of three separate but related civil actions in the Southern District of New York before Milton Pollack, *District Judge.*

In *Chris-Craft Industries, Inc.* v. *Piper Aircraft Corporation, et al.* (No. 72-1064), Chris-Craft appeals from the district court's dismissal after trial of its complaint against all defendants, 337 F.Supp. 1128 (S.D.N.Y. 1971), essentially on the grounds that many of the alleged securities laws violations had not been proven, that those proven had not caused injury to Chris-Craft and that Chris-Craft had failed to prove its claim for damages. We reverse and remand.

In *Bangor Punta Corporation* v. *Chris-Craft Industries, Inc.* (No. 72-1120), Bangor Punta appeals from the district court's dismissal after trial of its complaint, 337 F.Supp. 1147 (S.D.N.Y. 1971), on the ground of insufficient evidence to support Bangor Punta's claims that Chris-Craft had violated the securities laws or that such violations had caused injury to Bangor Punta. We affirm.

In *SEC* v. *Bangor Punta Corporation* (Nos. 72-1053 and 72-1140), the SEC appeals from those provisions of the

district court's judgment after trial, 331 F.Supp. 1154 (S.D.N.Y. 1971), which denied a permanent injunction against further violations of the securities laws and which imposed a condition upon Bangor Punta's rescission offer to former Piper shareholders. On the SEC's appeal, to the extent the judgment is appealed from, we affirm in part, and reverse and remand in part. On Bangor Punta's cross-appeal, we affirm.

I.

EVENTS LEADING TO INSTANT LITIGATION

Before turning to the issues raised on appeal in each of the three actions, we shall set forth a narrative of the events, beginning in the latter part of 1968 and during 1969 in connection with the contest for control of Piper Aircraft Corporation, which culminated in the instant litigation. Facts having specific bearing upon the issues in each of the three appeals will be discussed in more detail in connection with our rulings below on those issues in each case.[1] Our task on these appeals has been greatly facilitated by Judge Pollack's detailed, comprehensive findings of fact, and particularly by his evaluation of the facts as found. While we disagree with certain of his conclusions, as will appear below, we take this occasion to com-

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1 The facts are substantially undisputed.

We shall assume familiarity with the detailed statements of facts set forth in the prior reported opinions involving this contest for control of Piper. In addition to the three opinions of Judge Pollack referred to above (337 F.Supp. 1128, 337 F.Supp. 1147, 331 F.Supp. 1154), there was an earlier opinion by Judge Tenney denying Chris-Craft's motion for a preliminary injunction (303 F.Supp. 191 (S.D.N.Y. 1969)), and an en banc opinion by this Court affirming the denial of the preliminary injunction, indicating certain violations of the securities laws and remanding to the district court for further proceedings not inconsistent with this Court's opinion. *Chris-Craft Industries, Inc.* v. *Bangor Punta Corp.*, 426 F.2d 569 (2 Cir. 1970) (en banc).

mend him upon the clarity of his opinions in these complex cases.

Chris-Craft Industries, Inc. (CCI) is a Delaware corporation. It is a diversified manufacturer of recreational products. Its securities, common and preferred stock and convertible debentures, are traded on the New York Stock Exchange (NYSE).

Piper Aircraft Corporation (Piper) is a Pennsylvania corporation. It is one of the nation's leading manufacturers of light aircraft. Its 1,644,890 shares of issued and outstanding stock were traded (during periods relevant to these appeals) on the NYSE from October 1, 1968 to August 11, 1969 and then on the Philadelphia-Baltimore-Washington Stock Exchange. The three individual Piper defendants (referred to herein as the "Piper family") were officers and directors of Piper and owned about 325,000 of the 1,644,890 outstanding Piper shares.

Bangor Punta Corporation (BPC) is a Delaware corporation. It is a conglomerate with holdings in diversified fields. Its securities are traded on the NYSE. Defendants Nicolas M. Salgo and David W. Wallace are principal officers and directors of BPC.

The First Boston Corporation (First Boston) is a Massachusetts corporation. It is an investment banking firm and also a registered broker-dealer. In connection with the events involved herein, it served as investment adviser to Piper and as underwriter for BPC. Defendant Paul L. Miller is president of First Boston and defendant Nicholas H. Bayard is a vice president in its underwriting department.

In the latter part of 1968, CCI undertook a large financing program designed to produce excess cash that could be used primarily for acquisitions. On October 30, 1968, CCI filed a registration statement and preliminary prospectus for

an offering of 6% convertible debentures up to $26 million in principal amount. The offer was made to shareholders and executives of CCI. It was largely successful, producing over $25 million in excess cash. At about the same time, Herbert Siegel, CCI's president and chief executive officer, discussed with the Philadelphia National Bank the obtaining of a revolving line of credit of up to $15 million. Such credit was granted and was drawn upon in February 1969 when needed.

CCI made its first purchase of Piper stock on December 30, 1968.[2] The purchase totalling 5200 shares was made through a confidential numbered account at Mitchell, Hutchins & Co., Inc., a member of the NYSE and a registered broker-dealer retained primarily by institutional investors. Additional purchases of Piper stock were made through Mitchell, Hutchins shortly thereafter in 1969:

January 3	36,100 shares (34,200 from Madison Fund at $54)
January 6	22,000
January 7	700
January 8	30,900 (all but 200 from Keystone Growth Fund)

CCI also made market purchases of Piper stock in the following amounts through other brokers:

January 14	3,700 shares
January 20	800
January 21	3,200

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2 CCI as of this date apparently had not yet decided to seek a controlling interest in Piper. Mr. Siegel testified that he had decided to buy the 5200 shares only a few days in advance and that he had not yet determined that an attempt to take over Piper would be advisable. The Board of Directors of CCI did not openly discuss the acquisition of Piper until its January 23, 1969 board meeting.

On January 22, CCI negotiated the purchase of 101,100 shares of Piper stock from Technology Fund, Inc. at $65 per share. This brought its total holdings in Piper to over 200,000 shares, approximately 13% of the outstanding Piper shares.

Up to this point, CCI had not officially informed Piper of its extensive purchases of Piper stock, nor had a public announcement been made.[3] On the morning of January 23, Mr. Siegel telephoned Mr. W. T. Piper, Jr., then President of Piper, and informed him that CCI would be announcing that day a cash tender offer for the purchase of Piper stock and that CCI had tentative plans to acquire a majority shareholder interest in Piper. In a statement released to the press that day, CCI announced a cash tender offer beginning immediately and ending on February 3 for up to 300,000 shares of Piper at $65 per share. The price of Piper stock on the NYSE at the close of January 22 was $52.50. CCI also revealed in its press release of January 23 that it was purchasing the stock for investment with a view to control of Piper, but that it did not presently have any specific plan or proposal with respect to the future of Piper.

The first response of the Piper management (essentially the Piper family) to the tender offer was to call a meeting on January 23 of representatives of First Boston (Piper's investment adviser), Chadbourne, Parke, Whiteside and Wolff (Piper's legal counsel), and Arthur Young & Co. (Piper's auditors). The next day, January 24, the Piper family decided to oppose CCI's bid for control of Piper. First Boston was asked to contact other companies to

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3 Section 13(d)(1) of the Securities Exchange Act of 1934, 15 U.S.C. §78m(d)(1) (1970), requires that certain reports be filed by a purchaser when he has acquired more than 10% of the outstanding stock of a company. CCI satisfied this requirement by filing a Schedule 13D with the SEC along with its tender offer materials.

solicit proposals which might be preferable to a CCI takeover. BPC was one of the companies contacted. It showed considerable interest. But Piper did not follow up at that time.

The Piper family's resistance to the CCI tender offer took several forms. On January 25, the Piper Board adopted a resolution that CCI's offer was not in the best interests of the Piper shareholders and decided that this resolution should be sent to them. Letters were sent out the same day asking Piper shareholders to delay accepting the CCI offer until the Piper management could adequately respond to it. This was followed by a letter dated January 27 over the signature of W. T. Piper, Jr.[4] The letter stated, among other things, that the Piper Board "has carefully studied this offer and is convinced that it is inadequate and not in the best interests of Piper's shareholders."

Also on January 25, Piper officers met with officers of Grumman Aircraft Engineering Corporation (Grumman) to discuss the sale of 300,000 unissued but authorized Piper shares to Grumman at $65 per share. An agreement was entered into on January 28 under which Grumman agreed to purchase 300,000 Piper shares at $65 per share; Piper agreed to seek approval from the NYSE for the listing of the new shares; and Grumman agreed to tender a check for $19,500,000 at a closing to be held within 3 days of the NYSE approval. The agreement was entered into with "the intention of Grumman and Piper to explore the desirability of a merger of their two corporations". Under the agreement, Grumman was given an option to put the shares back to Piper after six months at Grumman's cost plus 3½% interest per annum running from the closing

4 This letter was prepared by D. F. King & Co. It was reviewed by the Piper family, by its legal counsel and by Mr. Bayard of First Boston.

date. In order to guarantee the option, Piper was required to maintain the proceeds of the sale in a fund separate from its other assets and free of liens. A press release was issued by Piper on January 29 announcing that Grumman "has agreed to purchase" 300,000 shares of Piper subject to the approval of the Boards of both companies. The release further stated that the agreement was also conditioned on the shares being listed with the NYSE, on there being no material adverse change in Piper's business, and on there being no change in the management of Piper. A letter tracking the language of the release was sent to Piper shareholders on the same day. There was no mention of the "put" arrangement in either the press release or the letter to shareholders. The Grumman agreement was terminated by mutual consent on March 19 after the NYSE advised the parties that it would not list the new shares.

Returning to CCI's program for purchasing Piper stock, its tender offer resulted in its acquiring an additional 304,606 shares of Piper. This boosted CCI's total holdings[5] to 547,106 shares, or approximately 33% of the outstanding shares of Piper as of February 3. To obtain the additional 17% necessary for control, CCI decided to make an exchange offer. On February 14, the Board of CCI approved the making of an exchange offer without determining its terms. On February 27, CCI filed with the SEC an S-1 registration statement and a preliminary prospectus for an exchange offer to acquire a minimum of 80,000 and a maximum of 300,000 Piper shares. CCI issued a press release on May 7 announcing the specific package of CCI securities to be exchanged for Piper shares. First Boston

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5 While the tender offer was outstanding, CCI continued to purchase Piper stock on the market. On January 24, 16,200 shares were purchased. Between January 27 and February 3, another 22,600 shares were purchased.

estimated that the package was worth $70-74 per Piper share. On May 12 and 16, the Board of CCI adopted resolutions approving the exchange offer and increased the value of the package by adding $10 cash.

Between March 18 and April 7, CCI had issued orders to Mitchell, Hutchins to continue purchases of Piper stock for CCI's account. CCI actually purchased 9100 shares while its exchange offer was being processed. On April 7, however, Mr. Siegel met with the SEC which warned him that such purchases violated Rule 10b-6 as the SEC interpreted it. Mr. Siegel informed the SEC that CCI would cancel all outstanding orders and it did.

In the meantime, the Piper management continued to search for an effective maneuver to defeat CCI. On March 22, Piper entered into an agreement with United States Concrete Pipe Company of Florida to acquire all the outstanding shares of Concrete Pipe in exchange for 320,000 authorized but unissued Piper shares. On the same day, Piper agreed to acquire 99.466% of the shares of Southply, Inc. in exchange for 149,199 authorized but unissued shares of Piper. Piper apparently hoped that, by increasing the number of Piper shares outstanding, CCI would find Piper less attractive. The NYSE refused to list the new shares because the Piper family had failed to obtain the approval of Piper shareholders for the deals. When Piper itself issued the stock certificates, an extremely unconventional procedure, the NYSE suspended trading in Piper stock beginning April 7 and initiated delisting procedures. Piper rescinded the agreements on April 14.

Going back for a moment to CCI's program for purchasing Piper stock, its tender offer between January 23 and February 3 had resulted in its bringing its total holdings of Piper shares to 547,106 or roughly one-third of Piper's outstanding shares (including those privately purchased). Pursuant to its February 27 exchange offer (which termi-

nated July 24), CCI acquired 39,826 additional Piper shares. And pursuant to its July 24 exchange offer (announced on May 7, approved by the CCI Board on May 12 and 16, and terminated on August 4), CCI acquired 112,089 additional Piper shares—thus bringing its total holdings of Piper shares to 668,295 or 41% of Piper's outstanding shares.

BPC's first contact with the contest for control of Piper came on January 24 when First Boston spoke to Nicolas M. Salgo, BPC's Chairman of the Board, about the possibility of a deal between Piper and BPC. Mr. Salgo showed some interest but Piper broke off contact until February 24 when there was a meeting of Piper and BPC representatives concerning a merger of the two companies. BPC officials demanded that the Piper family sell to BPC all its holdings in Piper, which amounted to 31% of the outstanding shares. The Piper family gave no answer at that time. Further meetings were held on April 18 and 20. The Piper family did not decide to sell until late April or early May.

On May 8, a formal agreement was entered into between BPC and the Piper family. BPC made a "limited exchange offer" of specified BPC stock, warrants, and debentures (valued by First Boston at $70-72 per Piper share), for the total Piper family holdings of Piper stock, 501,090 shares. BPC also promised to use its best efforts to acquire additional stock to bring its holdings up to more than 50% of the outstanding Piper stock by a "further exchange offer" of "Bangor Punta securities and/or cash having a value, in the written opinion of the First Boston Corporation, of $80 or more per Piper share". It was further agreed that if BPC were successful in gaining control of Piper, and if First Boston determined that the package of securities received by the Piper family were valued at less than $80 on the opening day of the general

exchange offer, the Piper family would be given stock and/or cash to make up the difference.

On May 8, a statement was released to the press by both Piper and BPC disclosing that BPC was acquiring the Piper family's stock holdings through an exchange offer for a package of BPC securities. The release contained a statement that BPC would offer to the remaining Piper shareholders a package of BPC securities to be valued in the judgment of First Boston "at not less than $80 per Piper share". This $80 valuation was repeated by David W. Wallace, President of BPC, to a reporter for the Wall Street Journal on May 16.

On May 26, the SEC brought an action against Piper and BPC in the District Court for the District of Columbia charging that the May 8 press release violated §5(c) of the Securities Act of 1933, 15 U.S.C. §77e(c) (1970), and Rule 135, 17 C.F.R. §230.135 (1972), in that the release constituted an offer to sell securities before any registration statement had been filed, the $80 valuation having overstepped the Rule 135 exemption (a contention with which our Court agreed in its earlier en banc decision, 426 F.2d at 574). Both defendants consented to a permanent injunction without admitting any of the allegations of the complaint.

On May 16, BPC filed with the NYSE and the SEC a Schedule 13D describing the May 8 agreement. On May 29, BPC filed an S-1 registration statement for both of the exchange offers, and also filed a preliminary prospectus for the "further exchange offer". The May 29 offering, described as a tentative offering, was as follows:

1 share of BPC common

Series C warrants expiring 3-31-81 to purchase 3.25 shares of BPC common at $55

$15 principal amount of new 5½% convertible subordinate debentures, due 1994, convertible at $55

While awaiting SEC action on the exchange offer, BPC negotiated cash purchases of a total of 120,200 shares of Piper stock in the following private transactions: On May 14, BPC purchased 78,600 Piper shares from Fund of Funds Proprietary Fund, Inc. in Nassau at $79.25 per share. On May 15, BPC purchased an additional 20,000 Piper shares for $74.25 per share from American Securities Corporation. On May 16, 20 and 23, in three separate transactions, BPC purchased from Bay Securities Corporation the following Piper shares at the prices indicated:

May 16	2,300	$76
	700	75.95
May 20	11,200	76.25
May 23	2,200	76.37
	5,200	78.37

All these purchases were made in disregard of SEC Exchange Act Release No. 8595, issued May 5, 1969, announcing proposed Rule 10b-13. This Rule, when adopted, would specifically prohibit BPC's purchases because they were made during the pendency of an exchange offer for the purchased shares. The Release stated that "[t]his provision is, in effect, a codification of existing interpretations under Rule 10b-6."

The Piper family naturally supported the BPC exchange offer and took several steps to ensure its success. On June 4, a letter over the signature of W. T. Piper, Jr. was sent to all Piper shareholders urging them to read and study carefully the preliminary prospectus on the BPC exchange offer. Another shareholder letter was sent on June 20 extensively criticising the CCI exchange offer and suggesting that the offer "is not in your best interests". Finally, on July 25, a week after the BPC offer had become effec-

tive, W .T. Piper, Jr. sent another letter to shareholders strongly recommending the BPC offer; it stated that the Piper management had been impressed with the BPC management and operations and that a combination with BPC would be in the best interests of all shareholders.

BPC did not fix the final terms of its exchange package until July 18, the day it became effective. The final offer consisted of the following securities:

1.2 shares of BPC common
Warrants for 3.5 shares of BPC common
$31 principal amount of new 8¼% convertible subordinate debentures, due 1994, convertible at $55

On July 18, First Boston sent to BPC an opinion letter which valued the combination of BPC securities at not less than $80 per Piper share based on market and other conditions existing prior to the opening of business on that day. Neither the preliminary nor the final prospectus on the BPC exchange offer—nor the First Boston opinion letter—referred to BPC's negotiations with another company for the sale of the Bangor and Aroostook Railroad, a major asset of BPC, for $5 million, which was $13.5 million less than the amount at which it was carried on the books. We shall discuss this more fully below.

To summarize CCI's public offers, on January 23, CCI had made its first tender offer for 300,000 Piper shares. By February 3, these efforts, together with its negotiated purchases, had gained CCI approximately 33% of the then outstanding Piper shares. On February 27, CCI filed with the SEC a registration statement and proposed prospectus for an exchange offer for a minimum of 80,000, a maximum of 300,000, additional Piper shares: after the period of this exchange offer had been extended six times, it finally was withdrawn on July 24 when CCI failed to obtain the minimum 80,000 shares. Still another exchange offer was

announced by CCI on May 7, adding substantially more value to its earlier package; a new registration statement for this exchange offer was filed with the SEC on July 22; and a new prospectus was filed on July 24, the effective date of the offer.

The BPC exchange offer expired on July 29 with BPC acquiring 111,628 shares. CCI's second offer expired on August and produced 112,089 shares.

The contest for control was not yet over, however, because after the expiration of both offers CCI and BPC owned only 41% and 45%, respectively, of the outstanding Piper shares. CCI made additional purchases of 29,200 shares between August 12 and 18, and then virtually withdrew from the struggle. BPC, on the other hand, continued to purchase for cash on the NYSE until August 11, and then purchased on the PBWSE until September 5. By September 5, it had acquired another 100,614 shares, enough to achieve a majority stockholder position in Piper (839,306 shares or 51%).

CCI had lost the battle for control after investing more than $44 million—$38,295,238 in cash and $6,333,029 in other forms of consideration such as stocks and warrants.

II.

CHRIS-CRAFT INDUSTRIES, INC. v. PIPER AIRCRAFT CORPORATION, ET AL. (NO. 72-1064)

On May 22, 1969, while the contest for control of Piper was still being waged, CCI brought this action in the District Court for the Southern District of New York. The amended complaint alleged violations of Section 5(c) of the Securities Act of 1933, 15 U.S.C. §77e(c) (1970), and Rule 135 promulgated under the 1933 Act, 17 C.F.R. §230.135 (1972); it also alleged violations of Sections 9,

10(b) and 14(e) of the Securities Exchange Act of 1934, 15 U.S.C. §§78i, 78j(b) and 78n(e) (1970), and Rules 10b-5 and 10b-6 promulgated under the 1934 Act, 17 C.F.R. §§240.10b-5 and 240.10b-6 (1972). The complaint sought damages and equitable relief.

On July 22, CCI moved for a preliminary injunction to prevent BPC from gaining and exercising control of Piper. Judge Tenney denied CCI's motion for a preliminary injunction on the grounds that CCI had failed to establish either irreparable injury if the motion were denied or unlawful conduct on the part of BPC. 303 F.Supp. 191.

An expedited appeal from Tenney's order resulted in an en banc decision by this Court. *Chris-Craft Industries, Inc.* v. *Bangor Punta Corp.*, 426 F.2d 569 (2 Cir. 1970). We held, in an opinion written by Judge Waterman, that a preliminary injunction was not required because BPC had stipulated upon oral argument not to effect a merger before the end of the litigation and we could perceive no other irreparable harm. We also ruled on the district court's alternative holding that the securities laws had not been violated, "for it [was] clear that this ruling below would determine the outcome of the trial on the merits." *Id.* at 573. We held that the May 8 press release violated §5(c) of the 1933 Act and Rule 135;[6] and that BPC's cash purchases of large blocks of Piper stock in May violated Rule 10b-6, but we made no determination whether the latter transactions were exempt under Rule 10b-6(a)(3)(2), which we discuss more fully at pages 4959-4963, *infra*. We remanded to the district court for proceedings not inconsistent with our opinion.

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6 The release was an "offer to sell" because it contained a statement of value and it was unlawfully issued prior to the filing of a registration statement.

On remand, CCI limited its claim for relief to damages, foregoing any claim for equitable relief.[6a] After trial on the merits before Judge Pollack, the district court filed an opinion. 337 F.Supp. 1128. The court found no merit in CCI's contentions that the Piper management misled the public by its January 23 letter which stated that CCI's cash tender offer was "inadequate", that the announcement of the Grumman agreement was deceptive because it failed to disclose the "put" provision, or that other January communications were misleading. The court rejected CCI's claim that the May 8 release was inaccurate, if "taken in its own terms". It found that, although the release violated §5(c) of the 1933 Act, CCI had failed to show that this violation caused it to lose the contest or to increase unnecessarily its cost of acquiring Piper stock. The court held that the BPC registration statement for its exchange offer was "unintentionally in error" in failing to disclose the negotiations for the sale of the Bangor and Aroostook Railroad, but that CCI had failed to prove the scienter and causal effect necessary for a Rule 10b-5 or §14(e) cause of action for damages brought by a party in the position of CCI. The court held that BPC's May cash purchases had violated Rule 10b-6 and were not exempt, but that the violations did not cause injury to CCI. The court faulted Piper for failing to disclose certain matters in its annual statements and other reports, but decided that CCI was not in a position to complain. With regard to the claims against First Boston, the court concluded that First Boston had not engaged in any conduct which operated as a fraud upon CCI or the public shareholders of Piper and that it should not be held liable for the actions of its client. The court held that Piper had failed to prove its counterclaim

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6a CCI also amended its complaint to allege violations of §16 of the 1934 Act, 15 U.S.C. §78p (1970).

against CCI by not adequately showing violations of the law or that such violations were related to injury sustained by Piper. The court dismissed CCI's complaint against the corporate defendants and against each of the individual defendants.[7]

For the reasons stated below, we reverse and remand with directions to grant appropriate relief.

(A) Function of Private Action for Damages in Enforcement of Federal Securities Laws

In order better to understand our rulings on the issues raised on this appeal—including our disagreement with the district court on certain issues—we believe it may be helpful briefly to delineate the proper function of the private action for damages in the overall pattern of enforcement of the federal securities laws.

This matter is squarely raised by the following observation by the district court in ruling on CCI's claims of violations of the antifraud provisions of the securities laws:

> "In effect, Chris-Craft seeks the windfall of a punitive award against Bangor Punta by assuming the role of defender of the public interest in the purity of the registration process. This role has already been assumed by the Commission and we could well expect it to be assumed by exchanging Piper holders if there were material harm to them." 337 F.Supp. at 1139.

The SEC of course has been entrusted—by the statutes and implementing decisions—with the primary responsibility of protecting the public interest under the federal secu-

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7 On appeal, CCI does not claim damages for BPC's violation of §5(c) of the 1933 Act, and it has dropped its claim that Piper directly deceived CCI as a purchaser of Piper shares by false and misleading statements in Piper's financial and other reports.

Piper has not appealed from the dismissal of its counterclaim.

rities laws. But the Supreme Court, as well as other federal courts including our own, have recognized that vigorous enforcement of the federal securities laws, particularly the antifraud provisions, can be accomplished effectively only when implemented by private damage actions. In *J. I. Case Co.* v. *Borak*, 377 U.S. 426 (1964), the Supreme Court emphasized that private actions provide "a necessary supplement to Commission action" and that "the possibility of civil damages or injunctive relief serves as a most effective weapon in the enforcement" of the securities laws. 377 U.S. at 432. See *Fischman* v. *Raytheon Mfg. Co.*, 188 F.2d 783 (2 Cir. 1951); *Speed* v. *Transamerica Corp.*, 235 F.2d 369 (3 Cir. 1956).

This policy of vigorous enforcement through private litigation has been the instrument for forging many salutary developments in the securities fraud area, including a broadening of standing to sue and a relaxation of the elements of proof in a private action. A private right of action for damages has been implied for purchasers or sellers defrauded in violation of Rule 10b-5. *Kardon* v. *National Gypsum Co.*, 69 F.Supp. 512, 513-14 (E.D.Pa. 1946). Shareholders deceived by misleading proxy solicitations have been held to have a cause of action under §14(a) of the 1934 Act, 15 U.S.C. §78n(a) (1970). *J. I. Case Co.* v. *Borak*, *supra*. The scienter requirement in a Rule 10b-5 private damage action appears to have been reduced to a knowledge of falsity or reckless disregard for the truth standard by our decisions in *Heit* v. *Weitzen*, 402 F.2d 909, 914 (2 Cir. 1968), *cert. denied*, 395 U.S. 903 (1969), and *Globus* v. *Law Research Service, Inc.*, 418 F.2d 1276, 1290-91 (2 Cir. 1969), *cert. denied*, 397 U.S. 913 (1970), "to insure the maintenance of fair and honest markets in . . . [securities] transactions." Section 2 of the 1934 Act, 15 U.S.C. §78b (1970). The reliance standard also has been relaxed under certain circumstances; for example, if a material omission or misstate-

ment is proven, a presumption may be raised that the plaintiff relied on the deception to his detriment. See *Affiliated Ute Citizens of Utah* v. *United States*, 406 U.S. 128, 153-54 (1972) (Rule 10b-5 violation); *Mills* v. *Electric Auto-Lite Co.*, 396 U.S. 375, 385 (1970) (§14(a) violation). These are merely examples of innovations that have been prompted in substantial part by a uniform policy of encouraging vigorous enforcement of the securities laws through private litigation.

To understand the indispensability of private actions in the securities area, and the necessity for facilitating such litigation, it may be illuminating to focus upon the reasons Congress enacted the antifraud and antimanipulation provisions of the statutes. Obviously Congress was concerned about the plight of the average public investor who is at a serious disadvantage in dealing with persons possessing superior knowledge, skill and resources. But the public in the role of investor is only part of the picture. The integrity and efficiency of the securities markets are even more important since our entire economy is dependent upon these markets. The securities market performs the essential function of assessing the value that society places upon the efforts of a particular enterprise so that society can obtain the maximum amount of its preferred goods and services that our resources can produce. This function can be performed effectively only if the delicately calibrated balance of factors affecting demand and supply are allowed to have their impact upon the market place through an unrestricted flow of information and funds. See Crossland & James, *The Gods of the Marketplace: An Examination of the Regulation of the Securities Business*, 48 B.U.L. Rev. 515 (1968). The securities laws seek to prevent restrictions which distort the market's estimate of value. Considering the weighty interests at stake, Congress and the courts justifiably have outlawed

all unfair and deceptive practices related to the trading of securities and have encouraged private damage actions to implement the enforcement of the federal securities laws.[8]

(B) Violations of Antifraud Provisions of Section 14(e) of 1934 Act

We turn now to one of the key issues on these appeals: CCI's claim that each of the defendants violated Section 14(e) of the Securities Exchange Act of 1934. We hold that they did.

We shall discuss seriatum with respect to this claim each of the subordinate issues as briefed and argued by the parties, namely, (1) standing of CCI to sue for damages, (2) defendants' violations of Section 14(e), and (3) causation. Then, after discussing CCI's further claim of violations of Rule 10b-6, we shall take up the form of relief to be granted.

(1) *Standing of CCI to Sue for Damages*

CCI claims that defendants violated Rule 10b-5 or §14(e) when, during the pendency of CCI's attempt to take over Piper, BPC and Piper issued improper and misleading press releases, BPC filed an exchange offer registration statement with material omissions, and the Piper family sent out shareholder letters with material omissions and

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8 Discernment must be exercised in determining whether a particular violation of an antifraud provision brings into play the policy of vigorous enforcement with all its effects. The Supreme Court's recent decision in *Superintendent of Insurance* v. *Bankers Life & Casualty Co.*, 404 U.S. 6, 11-13 (1971), indicates that a Rule 10b-5 cause of action may be stated even though the fact that a security somehow was involved in the underlying transaction is otherwise insignificant. In such cases, although there may have been a securities law violation, the harm caused by the violation may not be regarded as sufficiently momentous to justify a dilution of the standards of proof normally required in an action for fraud.

misstatements. All the alleged violations relate either to a cash tender offer or to an exchange offer the purpose of which was to secure for the offeror a majority shareholder position in the target corporation.

Defendants contend that CCI lacks standing to complain of their alleged violations of Rule 10b-5 or §14(e).

The district court found it unnecessary to decide whether CCI had standing under Rule 10b-5 because there was a failure to show causation; and it found that it was "unnecessary to decide whether §14(e) may be separately invoked by one competitor for corporate control against another" since "our 10b-5 conclusions are dispositive of the issues as raised under Section 14(e)". 337 F.Supp. at 1134 and 1140.

We hold that CCI does have standing under §14(e) to sue defendants for damages. Our holding is based on the statute itself and such decisional law as there is that has touched on the question.

Section 14(e) of the Exchange Act, 15 U.S.C. §78n(e) (1970), provides:

> "It shall be unlawful for any person to make any untrue statement of a material fact or omit to state any material fact necessary in order to make the statements made, in the light of the circumstances under which they are made, not misleading, or to engage in any fraudulent, deceptive, or manipulative acts or practices, in connection with any tender offer or request or invitation for tenders, or any solicitation of security holders in opposition to or in favor of any such offer, request, or invitation."

The Senate Report which accompanied proposed §14(e) indicates clearly—more specifically than does Rule 10b-5[9]—

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9 Rule 10b-5 under the 1934 Act, 17 C.F.R. §240.10b-5 (1972), provides:

"It shall be unlawful for any person, directly or indirectly, by

that §14(e) was intended to make applicable to a tender offer the long established antifraud proscriptions of the federal securities laws:

> "Proposed subsection (e) would prohibit any misstatement or omission of a material fact, or any fraudulent or manipulative acts or practices, in connection with any tender offer, whether for cash, securities or other consideration, or in connection with any solicitation of security holders in opposition to or in favor of any tender offer. This provision would affirm the fact that persons engaged in making or opposing tender offers or otherwise seeking to influence the decision of investors or the outcome of the tender offer are under an obligation to make full disclosure of material information to those with whom they deal." S. Rep. No. 510, 90th Cong., 2d Sess. (1968), quoted in U.S. Code Cong. & Admin. News 2811, 2821 (1968).

See also *H. K. Porter Co.* v. *Nicholson File Co.*, —— F.Supp. ——, —— (D.R.I. 1972), 4 CCH Fed. Sec. L.Rep. ¶93,703, at 93,079-81 (Nov. 30, 1972).

Section 14(e) is especially appropriate where, as in the instant case, the tender offer, in connection with which fraud is charged, was made with a view to obtaining control of a target company. The Williams Act of 1968, of which §14(e) is a part, was enacted to control what has become

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the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

(a) To employ any device, scheme, or artifice to defraud,

(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(c) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security."

an increasingly popular method of corporate acquisition—obtaining a majority of a corporation's stock rather than its assets. See Mundheim, *Tender Offers*, 2 Rev. of Securities Reg. 953 (1969). The Act added to §13 of the 1933 Act subsections (d) and (e), which require tender offer disclosures similar to those required for issuance of new securities. Section 14(e) provides for openness and truthfulness in the solicitation of shares through tender offers and in the opposition to such solicitation.

Although the fraudulent acts involved in the instant case literally are proscribed by Rule 10b-5, we conclude that §14(e) is the antifraud provision which more appropriately provides the basis for CCI's standing to sue here. It therefore is unnecessary for us to decide whether CCI has standing to sue under §10(b) and Rule 10b-5.

A corporation in the position of CCI undoubtedly has standing to sue in a constitutional sense on the basis of the illegal acts alleged in the instant action.[10] Those who

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10 The issue of standing to which we address ourselves is whether CCI is an appropriate party to be seeking relief on account of defendants' illegal conduct. As stated in *Flast* v. *Cohen*, 392 U.S. 83, 99 (1968), quoting *Baker* v. *Carr*, 369 U.S. 186, 204 (1962), a threshold question is presented by the provision in Article III, Section 2, of the United States Constitution, limiting federal judicial power to cases and controversies:

> "The 'gist of the question of standing' is whether the party seeking relief has 'alleged such a personal stake in the outcome of the controversy as to assure that concrete adverseness which sharpens the presentation of issues upon which the court so largely depends . . . .'"

While a personal stake in the outcome meets the Article III requirement, a court must take into account other considerations before deciding that a plaintiff has standing to sue.

In the absence of a specific provision in a federal statute authorizing suit, the Constitution requires that we analyze the statute to ascertain whether a federal cause of action can be derived from it in favor of the plaintiff. See *Bivens* v. *Six Unknown Named Agents*, 403 U.S. 388 (1971). Depending on the statute, Congress may have intended, for any number of reasons, that only certain persons should be entitled to sue thereunder, and the plaintiff may not be one of them. See *Birnbaum*

make tender offers have an economic interest in restricting their opponents to fair conduct, for fear that they themselves might incur injury because of practices which they are legally barred from meeting in kind. CCI's allegations indicate that it has "a personal stake in the outcome of the controversy", *Baker* v. *Carr*, 369 U.S. 186, 204 (1962), because it has suffered a pecuniary loss directly attributable to the defendants' acts. See generally *Flast* v. *Cohen*, 392 U.S. 83, 94-101 (1968). Thus, under the requirements of the cases or controversies clause of the United States Constitution, CCI is an appropriate party to complain of such illegal acts.

We must also decide, however, whether CCI has a private federal right of action under §14(e) against each of the defendants and, more specifically, whether it has a claim for compensatory damages.[11] Cf. *Dyer* v. *Eastern*

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v. *Newport Steel Corp.*, 193 F.2d 461 (2 Cir.), *cert. denied*, 343 U.S. 956 (1952). On the other hand, Congress may have authorized the plaintiff to bring suit but limited the type of relief to which he is entitled. In short, the Constitution or statutory scheme enacted by Congress should be closely examined to determine whether the particular action brought by the plaintiff is explicitly or implicitly authorized.

The question whether a right of action or claim for relief exists under federal law is conceptually different from the *Flast* question. While attempting to make clear which concept we are discussing, we nevertheless shall refer to both as questions of "standing" since that is the term used in our prior decisions referring to §14(e). See, e.g., *Butler Aviation International, Inc.* v. *Comprehensive Designers, Inc.*, 425 F.2d 842, 843 n. 1 (2 Cir. 1970); *Crane Co.* v. *Westinghouse Air Brake Co.*, 419 F.2d 787, 798-99 (2 Cir. 1969), *cert. denied*, 400 U.S. 822 (1970); *Iroquois Industries, Inc.* v. *Syracuse China Corp.*, 417 F.2d 963, 969-70 (2 Cir. 1969), *cert. denied*, 399 U.S. 909 (1970); *Electric Specialty Co.* v. *International Controls Corp.*, 409 F.2d 937, 944-46, 948 (2 Cir. 1969).

11 A party with a sufficient economic or legal interest at stake conceivably might be permitted to bring an action to vindicate the public interest. That is, although his own interest was not intended to be protected by the statute, he might be allowed to sue, because of his own economic interest in the result, on behalf of those whose interests were to be protected. Cf. *FCC* v. *Sanders Bros. Radio Station*, 309

Trust and Banking Co., 336 F.Supp. 890, 913-14 (D.Maine 1971). The statute is silent as to a private remedy. In deciding this issue, however, we are not writing from a clean slate. Our Court has spoken on the issue on at least four previous occasions. In *Electronic Specialty Co.* v. *International Controls Corp.*, 409 F.2d 937, 940-41, 944-46 (2 Cir. 1969), our holding on the merits made it unnecesssary for us to reach a decision on the standing question, but we did indicate that a target corporation and nontendering shareholders could bring an action for a preliminary injunction under §14(e) against an offeror charged with wrongdoing. In *Butler Aviation International, Inc.* v. *Comprehensive Designers Inc.*, 425 F.2d 842, 843 n. 1 (2 Cir. 1970), a target corporation sought a preliminary injunction and we expressly held that standing existed under §14(e), at least as to the misstatements in the anual report. See also *Susquehanna Corp.* v. *Pan American Sulphur Co.*, 423 F.2d 1075 (5 Cir. 1970). In *Crane Co.* v. *Westinghouse Air Brake Co.*, 419 F.2d 787 (2 Cir. 1969), *cert. denied*, 400 U.S. 822 (1970), after holding that a tender offeror had a Rule 10b-5 claim for relief against a target corporation under the "forced seller" principle, we went on to say that:

> "The amendment to the Act adding section 14(e) (15 U.S.C. §78n(e)), . . . should serve to resolve any doubts about standing in the tender offer cases, even where an offeror is not, as is Crane, in the position of a forced seller." 419 F.2d at 798-99.

See also *H. K. Porter Co.* v. *Nicholson File Co.*, *supra*, 4 CCH Fed.Sec.L.Rep. at 93,079-81. In upholding the dis-

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U.S. 470, 476-77 (1940); *Mutual Shares* v. *Genesco*, 384 F.2d 540, 543-46 (2 Cir. 1967). But in such a suit by a "private attorney general", compensatory damages normally would be improper relief, although punitive damages might be permitted.

missal of a Rule 10b-5 claim in another action brought by an offeror against a target corporation, we suggested that standing might be provided by §14(e) although the 1968 amendment is an indication that "there was no standing to sue under Rule 10b-5 by either the tender offeror or by the target corporation". *Iroquois Industries, Inc.* v. *Syracuse China Corp.*, 417 F.2d 963, 969-70 (2 Cir. 1969), *cert. denied*, 399 U.S. 909 (1970).

While we have not heretofore squarely held that a private right of action for damages can be implied from §14(e) in favor of a party in CCI's position, we have indicated that such an implied right of action would be reasonable. Section 14(e) prohibits, as stated above, material omissions and misstatements in communications favoring or *opposing* tender offers. Under well recognized common law principles, interference with a "prospective advantage", such as the opportunity to purchase property, gives rise to a cause of action in the person injured where the means of interference adopted alone is unlawful, even though the purpose in itself may be justifiable. Prosser & Smith, Cases and Materials on Torts 1131-52 (1967). CCI therefore probably could state a claim for relief in most state courts against each of the defendants for tortious interference. Through unlawful and deceptive practices, they allegedly have denied CCI a fair opportunity to succeed in its tender offers. We will not infer from the silence of the statute that Congress intended to deny a federal remedy and to extinguish a liability which, under established principles of tort law, normally attends the doing of a proscribed act. See *Kardon* v. *National Gypsum Co.*, 69 F.Supp. 512, 513-14 (E.D. Pa. 1946).

We previously have noted, referring to §14(e), that "[t]he legislative history of the 1968 amendment demonstrates that the focus of legislative interest was on the public shareholder; Congress wanted to ensure that he had

the benefit of a full statement from the offeror, with a chance for 'incumbent management' to 'explain its position publicly', if so disposed, H.R. Rep. No. 1711, *supra*, at 2, U.S. Code Cong. & Adm. News at p. 2998." *Electronic Specialty Co.* v. *International Controls Corp., supra*, 409 F.2d at 945; *Susquehanna Corp.* v. *Pan American Sulphur Co., supra*, 423 F.2d at 1085. The general objective surely is to encourage extensive and accurate disclosure of information relevant to a tender offer. The Supreme Court made it clear in *J. I. Case Co.* v. *Borak, supra*, 377 U.S. at 432-33, that, in dealing with controversies involving the securities laws, we should not be reluctant to imply a private right of action when to do so will further the general objective of the statute involved. We can conceive of no more effective means of furthering the general objective of §14(e) than to grant a victim of violations of the statute standing to sue for damages. CCI is such a victim, as recognized by common law tort principles. A party in its position is especially likely to vindicate the wrong inflicted upon it. Particularly in light of the enforcement rationale of *Borak*, we believe it is both necessary and appropriate that CCI should be granted standing to sue for damages.

In enacting §14(e), while Congress did not explicitly state that shareholders of a target company are not the only persons entitled to the protection of the securities laws from fraudulent misrepresentations, it is a fair inference that a broader standing was intended. Since Rule 10b-5 covers all types of exchange offers, the major contribution provided by §14(e) would appear to be a broader standing to sue—accorded both to the offeror and to the opposition—based on fraudulent securities transactions. See *Bath Industries, Inc.* v. *Blot*, 427 F.2d 97, 102 (7 Cir. 1970); *Dyer* v. *Eastern Trust and Banking Co.*, 336 F.Supp. 890, 914 (D. Maine 1971). In *Electronic Specialty Co.* v.

International Controls Corp., supra, 409 F.2d at 940-41, we commented on the impact of §14(e):

> "In effect this applies Rule 10b-5 both to the offeror and to the opposition—very likely, except perhaps for any bearing it may have on the issue of standing, only a codification of existing case law."

While Judge Friendly's opinion in *Electronic Specialty* is not dispositive, its holding that the target company may sue goes some distance toward saying that contestants may also sue. Cf. *Iroquois Industries, Inc.* v. *Syracuse China Corp., supra*, 417 F.2d at 969-70.

Our holding on the standing of CCI to sue for damages may be summarized as follows. The statutory language of §14(e) is silent on standing; it neither confers nor excludes standing with respect to one in the position of CCI. As a distinguished commentator said years ago, in such a situation there is no need to try to discover "supposed legislative intent"; [w]hether his offenses shall have any other legal consequence has not been passed on one way or the other as a question of legislative intent, but is left to be determined by the rules of law." Thayer, *Public Wrong and Private Action*, 27 Harv. L. Rev. 317, 320 (1914). Under common law tort principles, we hold that a claim for relief under federal law is stated where, as here, a defeated contestant for control has been put in a minority shareholder position because of the wrongdoing of its opponent and the margin of victory is only 7%. CCI has shown that it had a reasonable chance of obtaining control of Piper, but lost the opportunity because its opponent gained control through means illegal under federal law. This is a case of first impression with respect to the right of a tender offeror to claim damages for statutory violations by his adversary. And our holding is

premised on the belief that the harm done the defeated contestant is not that it had to pay more for the stock but that it got less stock than it needed for control.

We hold that CCI has a right of action for damages against all defendants for violations of §14(e).[12]

(2) *Defendants' Violations of Section 14(e)*

The district court held that the various communications to shareholders by members of the Piper family and the May 8 press release by Piper and BPC did not violate §14(e), but that the BPC registration statement and prospectus were materially misleading. 337 F.Supp. at 1134-38, 1138-40. CCI challenges the court's holdings with respect to the Piper communications to shareholders and the May 8 press release. Defendants contend that the BPC registration statement and prospectus did not violate §14(e). We hold that each of the defendants violated §14(e).

(a) Controlling Principles In Determining Section 14(e) Violations

Before turning to defendants' alleged violations of Section 14(e), a statement of what we believe to be the controlling principles in determining such liability may aid in understanding our rulings which follow.

Section 14(e) is relatively new. It has not been the subject of extensive judicial construction, and never in the context of the factual situation here presented. And yet the underlying proscription of §14(e) is virtually identical

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12 The fraudulent acts alleged to have been committed by Piper and its allies, BPC and First Boston, in effect were in the nature of countersolicitations to CCI's tender offers. CCI's right of action against each therefore is the same: to recover damages or to obtain other relief based on defendants' illegal conduct under §14(e) to achieve an objective injurious to CCI.

to that of Rule 10b-5; the critical difference is that the latter is applicable only "in connection with the purchase or sale of any security", while the former is applicable "in connection with any tender offer . . . or any solicitation of security holders in opposition to . . . any such offer . . . ." In determining whether §14(e) violations were committed in the instant case, we shall follow the principles developed under Rule 10b-5 regarding the elements of such violations. In short, we hold that a violation of §14(e) is shown when there has been a material misstatement or omission concerned with a tender offer and when such misstatement or omission was sufficiently culpable to justify granting relief to the injured party. The key concepts in this formulation are *materiality* and *culpability.*[13]

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13 It is well to bear in mind Judge Friendly's observations regarding §14(e) in *Electronic Specialty Co.* v. *International Controls Corp., supra,* 409 F.2d at 948:

> "The likeness of tender offers to proxy contests is not limited to the issue of standing. They are alike in the fundamental feature that they generally are contests. This means that the participants on both sides act, not 'in the peace of a quiet chamber,' Hellenic Lines Ltd. v. Brown & Williamson Tobacco Corp., 277 F.2d 9, 13 (4 Cir.), cert. denied, 364 U.S. 879, 81 S.Ct. 168, 5 L.Ed 2d 102 (1960), but under the stresses of the market place. They act quickly, sometimes impulsively, often in angry response to what they consider, whether rightly or wrongly, to be low blows by the other side. Probably there will no more be a perfect tender offer than a perfect trial. Congress intended to assure basic honesty and fair dealing, not to impose an unrealistic requirement of laboratory conditions that might make the new statute a potent tool for incumbent management to protect its own interests against the desires and welfare of the stockholders. These considerations bear on the kind of judgment to be applied in testing conduct—of both sides—and also on the issue of materiality. As to this we reaffirm the test announced in *Symington Wayne, supra,* 383 F.2d at 843, whether 'any of the stockholders who tendered their shares would probably not have tendered their shares' if the alleged violations had not occurred. See also General Time Corp. v. Talley Industries, Inc., supra, 403 F.2d at 161-162."

The concept of materiality focuses on the weightiness of the misstated or omitted fact in a reasonable investor's decision to buy or sell. We articulated the materiality standard in *List* v. *Fashion Park, Inc.*, 340 F.2d 457, 462 (2 Cir.), *cert. denied*, 382 U.S. 811 (1965), to be "whether 'a reasonable man would attach importance [to the fact misrepresented] in determining his choice of action in the transaction in question.'" [14] The materiality test is concerned only with whether a prototype reasonable investor would have relied. See *Heit* v. *Weitzen*, 402 F.2d 909, 912-14 (2 Cir. 1968), *cert. denied*, 395 U.S. 903 (1969). Account must be taken of all the surrounding circumstances to determine whether the fact under consideration is of such significance that a reasonable investor would weigh it in his decision whether or not to invest. See *SEC* v. *Texas Gulf Sulphur Co.*, 401 F.2d 833, 849 (2 Cir. 1968) (*en banc*), *cert. denied sub nom. Kline* v. *SEC*, 394 U.S. 976 (1969).

As for the concept of culpability, intent to defraud is not an indispensable element in a private action under Rule 10b-5; knowledge of falsity or reckless disregard for the truth may be sufficient. See *Shemtob* v. *Shearson, Hammill & Co.*, 448 F.2d 442, 445 (2 Cir. 1971); *Globus* v. *Law Research Service, Inc.*, 418 F.2d 1276, 1290-91 (2 Cir. 1969), *cert. denied*, 397 U.S. 913 (1970); *Heit* v. *Weitzen, supra*, 402 F.2d at 913-14; *SEC* v. *Texas Gulf Sulphur Co., supra*, 401 F.2d at 854-55. We have indicated, however, that mere negligent conduct is not sufficient "to permit plaintiffs to recover damages in a private action under §17(a) or §10(b)." *SEC* v. *Manor Nursing Centers, Inc.*, 458 F.2d 1082, 1096 n. 15 (2 Cir. 1972).

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14 And in *SEC* v. *Texas Gulf Sulphur Co., supra*, 401 F.2d at 849: "[M]aterial facts include not only information disclosing the earnings and distributions of a company but also those facts . . . which may affect the desire of investors to buy, sell, or hold the company's securities."

The function of what has been called the "scienter" requirement is to confine the imposition of liability to those whose conduct has been sufficiently culpable to justify the penalty sought to be exacted. The initial inquiry in each case is what duty of disclosure the law should impose upon the person being sued. See *Royal Air Properties, Inc.* v. *Smith*, 312 F.2d 210, 212 (9 Cir. 1962); *Ellis* v. *Carter*, 291 F.2d 270, 274 (9 Cir. 1961). In making this determination we should bear in mind that a major congressional policy behind the securities laws in general, and the antifraud provisions in particular, is the protection of investors who rely on the completeness and accuracy of information made available to them. See 1 Bromberg, Securities Law: Rule 10b-5, §7.1, at 14 (1971). Those with greater access to information, or having a special relationship to investors making use of the information, often may have an affirmative duty of disclosure. When making a representation, they are required to ascertain what is material as of the time of the transaction and to disclose fully "those material facts about which the [investor] is presumably uninformed and which would, in reasonable anticipation, affect his judgment". *Kohler* v. *Kohler Co.*, 319 F.2d 634, 642 (7 Cir. 1963). A failure to perform these duties with "due diligence" in issuing registration materials provides a basis for suit under §11 of the 1933 Act, 15 U.S.C. §77k (1970). A knowing or reckless failure to discharge these obligations constitutes sufficiently culpable conduct to justify a judgment under Rule 10b-5 or §14(e) for damages or other appropriate relief against the wrongdoer. *SEC* v. *Texas Gulf Sulphur Co.*, *supra*, 401 F.2d at 854-55.

In sum, and put as simply as possible, the standard for determining liability under §14(e) on the part of a person making a misleading tender offer, or a responsible officer of a corporation making such such an offer, is whether

plaintiff has established that defendant either (1) knew the material facts that were misstated or omitted, or (2) failed or refused to ascertain such facts when they were available to him or could have been discovered by him with reasonable effort.

Our disagreement with the district court on whether defendants have violated §14(e) does not go to its findings of fact, as to which the "unless clearly erroneous" test applies, but to its application of the legal standards just discussed. See *Mamiye Bros.* v. *Barber S.S. Lines, Inc.*, 360 F.2d 774, 776-78 (2 Cir.), *cert. denied*, 385 U.S. 835 (1966).

We turn now to a consideration of the §14(e) violations charged against each of the defendants.

(b) Piper Family

CCI's charges against the Piper family stem from a series of communications to Piper shareholders in the form of shareholder letters and a press release.

The shareholder letters dated Januury 27 and 28, sent while the CCI tender offer was pending, stated that the Piper Board of Directors had "carefully studied this offer and is convinced that it is inadequate and not in the best interests of Piper's shareholders". It further stated that, if CCI were suddenly willing to offer shareholders $65, it must believe that Piper stock is worth more than it is offering.[15] CCI contends that a reasonable shareholder

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15 The letter also stated that Piper was talking to major industrial corporations about combination and that if one could be put through, "[A] higher value could be realized for all shareholders." This was not misleading because Piper officials were trying to find an alternative, such as a merger, that would be better for themselves and Piper shareholders. The letter also urged shareholders to consider "important points" such as the facts that "Piper's sales increased more than 20% in fiscal 1968 over the prior year, and its earnings per share were approximately 29% higher." CCI maintains that they should also have disclosed that sales and earnings for the first quarter of the next

would have assumed that "inadequate" referred to price. At that time Piper stock was selling on the market for considerably less than $65 per share. First Boston in fact had given Piper its opinion that the price offered was "fair and equitable". The Piper corporation itself, acting through the Piper family, at that time was contemplating a large sale of Piper stock to Grumman at the same price.

The district court concluded that "inadequate" referred to factors other than price, such as the quality of Chris-Craft management. We disagree. A reasonable shareholder reading the letter most likely would assume that the reference was to price. Since price usually is what a person contemplating a sale of shares is most concerned with, a prudent shareholder naturally would assume that the Piper family was addressing itself to that consideration in opposing the offer. If the Piper family intended to refer to other factors, it surely would have been more specific. The Piper family's culpability regarding these shareholder letters is clear. Corporate officers and directors in their relations with shareholders owe a high fiduciary duty of honesty and fair dealing. See *Swanson* v. *American Consumer Industries, Inc.*, 415 F.2d 1326 (7 Cir. 1969). By reason of the special relationship between them, shareholders are likely to rely heavily upon the representations of corporate insiders when the shareholders find themselves in the midst of a battle for control. Corporate insiders therefore have a special responsibility to be meticulous and precise in their representations to shareholders. The Piper family obviously disregarded this obligation when they sent out these shareholder letters knowing that they were materially misleading.

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fiscal year were down considerably compared to the first quarter of the previous year. We cannot say that, once Piper mentioned sales and earnings figures, it was required to reveal all relevant figures. Nor can we say that the decline was so severe that it made the previous year sales and earnings figures deceptive.

CCI also attacks the press release of January 29 by Piper officials that Grumman had "agreed to purchase" 300,000 shares of Piper at $65 per share. CCI argues that the tentative nature of the January 25 agreement was not adequately disclosed in the release. The agreement permitted Grumman to return the entire 300,000 shares for a refund of its purchase price plus interest within six months. This "put" provision was not disclosed in the press release, although it was described in Piper's application for listing with the NYSE. The release did reveal that the agreement was subject to the approval of the Piper and Grumman boards as well as other conditions. The published list of conditions gave the appearance of being exclusive, thus solidifying the impression that the sale was all but formally completed.

We find no fault in the Piper family's effort to avert through a Grumman merger what they had concluded was an unfavorable takeover by CCI. Such a maneuver is a common response to a takeover attempt. See Schmultz & Kelly, *Cash Take-Over Bids—Defense Tactics*, 23 Bus. Law 115, 132-34 (1967). We also agree with the district court's conclusions that the agreement was not a "sham" and that the "put" was a rational and logical part of the agreement. But Piper's failure to describe the put in its press release, or in its subsequent letter to shareholders, constituted a material omission in violation of §14(e). By failing to disclose this provision, the release portrayed the Grumman agreement as a completed, favorable deal between Piper and Grumman which also was likely to provide a basis for further and more profitable relations between the two companies.[16] The "agreement" actually was

16 This depiction of the agreement was further suggested by a statement in the release that the "purchase provides an opportunity for Grumman and Piper to study the feasibility and advantages of a possible combination of the two companies."

a preliminary and conditional overture directed toward a possible merger. The Piper family recklessly disregarded its obligation to shareholders in failing to disclose with substantial accuracy a transaction which was likely to affect the attitude of Piper shareholders toward the CCI tender offer.

CCI also challenges the shareholder letters with respect to the BPC and CCI exchange offers on the ground that they failed to disclose the Piper family's financial interest in the success of the BPC general exchange offer. Letters dated June 4 and July 25 urged Piper shareholders to accept the BPC exchange offer. A June 20 letter disparaged the CCI exchange offer. All the letters were sent over the signature of W. T. Piper, Jr. None of the letters explained that, under the terms of the May 8 agreement between BPC and the Piper family, the Piper family might profit handsomely from BPC's acquiring a controlling interest in Piper.[17] The agreement provided, as stated above, that, if the value of the securities package traded to the Piper family for their Piper holdings was below $80 per Piper share on the effective date of the general exchange offer, BPC would make up the difference, *if* BPC were successful in obtaining over 50% of the outstanding Piper shares. The Piper family therefore potentially had an interest in the success of the BPC exchange offer. By July 25, they must have realized that this interest amounted to a considerable sum of money.[18] If the letters merely had sup-

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17 The preliminary and final prospectus for the BPC general exchange offer disclosed that there had been an exchange offer made to the Piper family and related that under the May 8 agreement the family might gain from the success of the general exchange offer. We do not believe under the circumstances that disclosure in a detailed and extremely complex prospectus, which did not accompany the letters, fulfilled the Piper family's duty to reveal this material fact. Cf. *Mills v. Electric Auto-Lite Co.*, 403 F.2d 429, 433 (7 Cir. 1968), *vacated and remanded*, 396 U.S. 375 (1970).

18 One estimate placed the amount at a total of $13 million.

plemented the prospectus in providing publicity for the terms of the offer, there might be less basis for concern that the Piper family's self-interest was not disclosed. But the letters are replete with the personal opinions and recommendations of W. T. Piper, Jr. on the quality of the BPC securities and the management of BPC. The July 25 letter, sent after the Piper family must have known what they stood to gain in the event of a successful BPC takeover, stated that "we strongly recommend" the offer and "we have been impressed with the management and operations of Bangor Punta". Under these circumstances, the Piper shareholders were entitled to receive information sufficient to make an informed judgment on the weight to be given the personal recommendations of the Piper family. Cf. *SEC* v. *Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 197-201 (1963).

We hold that the communications to Piper shareholders in the form of shareholder letters and a press release constituted violations of §14(e) by the Piper family defendants.

(c) BPC And Its Officers

CCI's claims that BPC violated §14(e) arise from public communications and filed materials regarding the BPC general exchange offer. On May 8, Piper and BPC published a press release which stated that BPC had agreed

> "to file a registration statement with the SEC covering a proposed exchange offer for any and all of the remaining outstanding shares of Piper Aircraft for a package of Bangor Punta securities to be valued in the judgment of the First Boston Corporation at not less than $80 per Piper share."

CCI contends that this statement was materially misleading because a reasonable investor would have interpreted the

$80 value figure to be a guarantee of market value when the actual market value proved to be considerably less than $80. As stated above, we held in our earlier en banc decision that this statement of value violated §5(c) of the 1933 Act but we made no determination whether the statement also was misleading. 426 F.2d at 573-76. We did observe that a prospectus "would have eliminated the possibility, perhaps the probability, that some persons would have construed the $80 figure as referring to market value when that value was neither accurate nor intended". *Id.* at 575.

The district court concluded that "the language of the May 8 release could not be confused by reasonable men ... with offers intending or implying guarantees of market value." 337 F.Supp. at 1137 n. 9.[19] We agree. If the release were to be construed as a promise of future value, it would not be as a promise of market value. A reasonably knowledgeable investor is aware that the "value" of a security can refer either to the market or sales price of the security or to its worth as measured by the assets and earnings of the issuing company. The absence of the term "market value" in the release, as well as the fact that the valuation was to be "in the judgment of the First Boston Corporation", would suggest to a prudent investor that "value" here was to be based on an appraisal of assets and earnings.

The statement of value was not a fraud violation for another reason. It was not a material representation. A rational investor considering whether to take advantage of the BPC exchange offer after it became effective would not have been influenced by the earlier promise of value when the actual package had been disclosed to him for scrutiny and value determination. We therefore agree

19 The district court also held that even if a prudent investor might have interpreted "value" to mean market or resale value, the BPC package turned out to be worth $73 to $79, the difference between the promise and performance being "de minimis".

with the district court that the May 8 release has not been shown to have been damaging to CCI.

BPC contends that the district court erred in holding that the BPC registration statement was misleading. The district court, in *SEC* v. *Bangor Punta Corporation*, 331 F.Supp. at 1160-61, held that BPC's failure to disclose the circumstances which made the carrying figure for the Bangor and Aroostook Railroad (BAR) obsolete caused the registration statement to be misleading. BPC carried on its books its holdings in the BAR (98.7%) at $18.4 million. Although this amount was established through questionable accounting techniques, such techniques are not specifically attacked here.[19a] CCI does charge that BPC failed to disclose that it had negotiated for a sale of the BAR at a price substantially below $18.4 million. Some additional facts are necessary to an understanding of this claim.[20]

At the April 1, 1969 BPC board meeting, BPC had considered disposing of the BAR and had appointed a committee headed by Curtis Hutchins to study various methods of disposition. On May 12 and 15, Hutchins met with Frederic Dumaine, Chairman of the Board of Amoskeag, Inc., to discuss the possible sale of the BAR to Amoskeag. On May 12, Dumaine offered $5 million for the BAR. He indicated no preference for buying assets or stock. On May 15, Hutchins provided Dumaine with information on the BAR, such as the railroad's cash flow figures and balance sheet. Dumaine decided that he wanted to buy the stock. Hutchins met with his committee the same day. They agreed that a sale to Dumaine at $5 million would be

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19a Among other things, the increase in book value resulting from a revaluation of the BAR was credited directly to earned surplus, thus by-passing the income accounts. This is dubious accounting procedure.

20 A full discussion of the BAR incident is set forth by the district court in *SEC* v. *Bangor Punta Corporation*, 331 F.Supp. at 1156-60.

BPC's best course of action. At a BPC board meeting on May 21, Hutchins reported Dumaine's offer and his committee's recommendation.[21] He did not ask for approval of the sale but only for authority to continue negotiations. Nicolas M. Salgo, BPC's Chairman, suggested selling 51% of the BAR then and 49% later for a total consideration of $7 million. This proposal was rejected by Dumaine when it was later submitted to him. The BPC board resolved to study further the tax and accounting ramifications of the sale. On May 27, Hutchins and Dumaine formulated a letter of understanding concerning the sale. This was not signed by Hutchins. It stated that "you [Dumaine] and I have agreed . . . on the sale" at $5 million, but qualified this by noting that any understanding was subject to BPC board approval. Hutchins repeatedly explained to Dumaine that his authority was limited to exploring possibilities of divestiture and that he did not have the power to make a decision alone. On June 3, Hutchins met with the BPC management. They decided to table the matter while their tax and accounting departments studied the effect of selling assets rather than stock. On June 16, Hutchins informed Dumaine that the board refused to approve the letter of understanding. He further explained that the BPC management considered it essential that the legal and accounting effects of the transaction be studied, and that these investigations probably could not be completed for another two months because other matters (the exchange offer) had priority. Hutchins expressed to Dumaine his personal opinion that a deal would be made. On September 9, the board authorized Hutchins to make the sale to Amoskeag of BAR assets rather than stock, if possible, but basically with freedom to enter into the deal on whatever terms he decided were best. The agreement was entered

21 Hutchins presented three options to the board: sale, merger, or status quo. He and the board rejected the last two options.

into on October 2, 1969. This resulted in BPC sustaining a $13.8 million book loss, thus contributing to an $8,566,964 loss of net income for 1969 and to a reduction in retained earnings from $37.9 million at the end of fiscal 1968 to $20.5 million at the end of 1969.

The district court found that "the Bangor Punta directors could not [at the time of the exchange offer] have believed that the $18.4 million figure . . . any longer represented a responsible appraisal of market value of the BAR holding". 331 F.Supp. at 1161. It concluded that "[c]onsistency of fair disclosure required exposure of circumstances which so clearly rendered obsolete an appraisal made four years earlier". *Id.*

We hold, under the principles enunciated above for determining §14(e) liability, that BPC was required to disclose to Piper shareholders the circumstances surrounding the negotiations for a sale of the BAR, to apprise them with a reasonable degree of accuracy of the seriousness of such negotiations, and to inform them of the basic effect this might have on the operations of BPC. In *SEC* v. *Texas Gulf Sulphur Co., supra*, 401 F.2d at 849, we stated the standard of materiality to be applied where an event has not yet occurred but certain facts are known in advance:

> "[W]hether facts are material . . . when the facts relate to a particular event . . . will depend at any given time upon a balancing of both the indicated probability that the event will occur and the anticipated magnitude of the event in light of the totality of the company activity."

Hutchins and the other special committee members—Robertson, Stone, Siel—were highly knowledgeable about the BAR's affairs. Several had been past presidents of

the BAR and all had managed it in some capacity. These men had decided in May 1969 that a sale to Amoskeag was the only viable alternative. Certainly the BPC board was likely to be strongly influenced by their decision. The board in fact had taken a position favorable to the sale from the beginning and was primarily concerned with getting as much out of the sale as possible. The board knew that a merger of the BAR with another New England railroad was improbable. If they kept it, there would have to be substantial capital outlays of $5 million over the next five years to break even. Under these circumstances, by July the board must have realized that a sale of the BAR at a price substantially below its carrying value would be effected in the near future. A possible loss of $13 million, moreover, would have a sufficiently drastic impact on the financial position of BPC to justify disclosure even if the probability of a sale were less. The district court found that a sale of the BAR at $5 million would eliminate 36% of BPC's retained earnings and 12% of the shareholders' book equity.

In addition to the sales negotiations, there were other circumstances indicating that the book value of the BAR was obsolete and unrealistic. Since 1967, the management of BPC had been trying to dispose of the BAR, originally through a merger with another railroad. They apparently realized that the BAR did not have a promising future. The $5 million offer from Amoskeag was the only realistic offer that BPC had received. This alone demonstrated that the BAR was not worth anything close to $18.4 million. BPC's auditors reported on May 20 that a sale to Amoskeag at that price would be reported as an extraordinary loss of $13.5 million.

On the basis of these facts, the district court concluded that the registration statement was "unintentionally in error" and that the omissions were "mere negligence". It

further concluded that the requisite scienter for a private damage action had not been shown. We disagree.

The district court's findings of fact, supported by substantial evidence, do not warrant the conclusions that BPC's officers had decided to sell the BAR before the exchange offer became effective and had postponed consummation in order to avoid disclosure. Nor does the evidence show that BPC failed to disclose the sales negotiations in bad faith. As we have indicated above, however, intent to defraud is not an indispensable element in a private action for damages under the antifraud provisions of the federal securities laws. *Heit* v. *Weitzen, supra,* 402 F.2d at 913-14. The securities laws impose upon an offeror of an exchange offer a duty to act reasonably in discovering facts material to the offer as of the time of the transaction and in disclosing fully those material facts of which the offeree is presumably unaware and which ostensibly would influence his judgment. Cf. *Kohler* v. *Kohler Co., supra,* 319 F.2d at 642. Corporate officers have a reasonable area of discretion in determining how far to explore the facts and in deciding what facts need to be disclosed. So long as they operate within this area, the securities laws do not impose liability. In order to encourage candor in the securities market, and well informed decisions by investors, this discretion must be exercised with caution.[22]

We believe that the officers of BPC greatly transgressed their allowable area of discretion in not disclosing the BAR negotiations and other circumstances reflecting the value of the BAR. The officials in charge of the exchange offer

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22 We do not hold that a corporation prima facie has acted unreasonably if the omission or misstatement is material. Corporate officials must be allowed considerable room for discretion; otherwise their normal functions as corporate officials will be inhibited. The totality of the facts and circumstances must be examined to determine whether the officials were reckless or grossly negligent.

were well aware of the discussions with Amoskeag and the activities of the special BAR committee. They also were aware of all the other circumstances that indicated that the book value of the BAR was deceptive and unrealistic. Their judgment not to reveal basic information about the then current status of the BAR holdings clearly was unreasonable. They showed reckless disregard for the import of their activities concerning the BAR. They knew that the book value of the BAR set forth in the registration statement was no longer realistic. Considering the totality of the facts and circumstances, they failed to discharge their clear duty of proper disclosure.

We hold that such conduct on the part of BPC and its officers violated §14(e).

(d) First Boston And Its Officers

CCI's claim that First Boston violated §14(e) is based on its conduct in connection with the BPC exchange offer. First Boston was the underwriter and dealer-manager for the exchange offer. As such, it had ready access to the books and records of BPC. It availed itself of this privilege sufficiently to examine the minutes of the BPC board meetings, including those of April 1 and May 21. Representatives of First Boston did not see the letter of understanding between Hutchins and Dumaine. They did question BPC's management regarding the BAR and were informed that there were no plans at the time to dispose of the railroad. That appears to have been the full extent of First Boston's investigation.

The federal securities laws impose upon private parties the primary responsibility for verifying the accuracy and completeness of information provided to potential investors. See H.R. Rep. No. 85, 73rd Cong., 1st Sess. 2-3 (1933). For this reason, Section 11 of the Securities Act

of 1933, 15 U.S.C. §77k (1970), authorizes the purchaser of a security to sue the underwriter and others involved in the issuance of securities, if the registration statement contains a misstatement or misleading omission of material fact. A "due diligence" defense to such a suit is available to all but the issuer. Section 11(b), 15 U.S.C. 77k(b) (1970), provides that a defendant can escape liability if he can prove that:

> "he had, after reasonable investigation, reasonable ground to believe and did believe, at the time such part of the registration statement became effective, that the statements therein were true and that there was no omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading."

Section 11 of course provides a cause of action only for a purchaser of securities issued pursuant to a registration statement. We believe that §14(e) imposes liability upon an underwriter in favor of a competing offeror, specifically where the misrepresentation occurs in the context of a contest for control. An underwriter is liable under §14(e) as an aider and abettor of the issuer if he was aware of a material falsity in the registration statement or was reckless in determining whether material falsity existed. See *SEC* v. *North American Research & Development Corp.*, 424 F.2d 63, 81 (2 Cir. 1970); Ruder, *Multiple Defendants in Securities Law Fraud Cases: Aiding and Abetting, Conspiracy, In Pari Delicto, Indemnification, Contribution,* 120 U. of Pa. L. Rev. 597, 620-46 (1972).

Section 14(e) provides that "[i]t shall be unlawful for any person to *make* any untrue statement of a material fact" or to mislead by omitting "to state any material fact". (Emphasis added). An underwriter or dealer-man-

ager for a securities issue does not actually prepare the registration materials. Thus, in a literal sense, it does not "make" statements to potential investors. But we do not read §14(e) so narrowly. An underwriter by participating in an offering constructively represents that statements made in the registration materials are complete and accurate. The investing public properly relies upon the underwriter to check the accuracy of the statements and the soundness of the offer; when the underwriter does not speak out, the investor reasonably assumes that there are no undisclosed material deficiencies. The representations in the registration statement are those of the underwriter as much as they are those of the issuer.

Self-regulation is the mainspring of the federal securities laws. No greater reliance in our self-regulatory system is placed on any single participant in the issuance of securities than upon the underwriter. He is most heavily relied upon to verify published materials because of his expertise in appraising the securities issue and the issuer, and because of his incentive to do so. He is familiar with the process of investigating the business condition of a company and possesses extensive resources for doing so. Since he often has a financial stake in the issue, he has a special motive thoroughly to investigate the issuer's strengths and weaknesses. Prospective investors look to the underwriter—a fact well known to all concerned and especially to the underwriter—to pass on the soundness of the security and the correctness of the registration statement and prospectus. See generally Note, *Escott* v. *Barchris: "Reasonable Investigation" and Prospectus Liability Under Section 11 of the Securities Act of 1933*, 82 Harv. L. Rev. 908 (1969). The Senate Report that accompanied proposed §14(e) indicates that this degree of involvement by the underwriter in the making or opposing of

a tender offer may subject him to liability if the registration materials are misleading:

> "This provision would affirm the fact that persons *engaged* in making or opposing tender offers or *otherwise seeking to influence* the decision of investors or the outcome of the tender offer are under an obligation to make full disclosure of material information to those with whom they deal". (Emphasis added). S. Rep. No. 510, 90th Cong., 2d Sess. (1968), quoted in U.S. Code Cong. & Admin. News 2811, 2821 (1968).

We turn now to a determination of whether First Boston violated §14(e). Since we already have concluded that the BPC registration statement and prospectus were materially deficient, the remaining issue to be determined is First Boston's culpability. First Boston is a skilled, experienced and well respected dealer-manager and underwriter. It had an obligation with respect to the BPC exchange offer to reach a careful, independent judgment based on facts known to it as to the accuracy of the registration statement. Moreover, if it was aware of facts that strongly suggested, even though they did not conclusively show, that the registration materials were deceptive, it was duty-bound to make a reasonable further investigation.

We hold that First Boston did not adequately perform its duty in these respects. The minutes of the April 1 and May 21 board meetings,[23] which were examined by the

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23 In view of the critical bearing these minutes have upon the issue of First Boston's liability, we set forth the relevant portions.

The minutes of the BPC board meeting of April 1, 1969 included the following reference to the BAR (Appendix 763):

> "ORGANIZATION AND LONG RANGE PLANNING.
>
> Mr. Salgo* stated that he wished to discuss with the Board the general philosophy of the types of business in which Bangor

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* Chairman of the Board.

underwriting department of First Boston, disclosed the early discussions and negotiations concerning the disposition of the BAR. At the April 1 meeting, the board considered disposing of the BAR and appointed a committee to study the alternatives. At the May 21 meeting, a pos-

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Punta should be involved, and also share with the Board some of the thoughts of management in this connection. He stated that there had been under consideration for some time the question of whether minority interests in some of the more attractive operations, such as the Leisure Time and Public Security Groups, should be spun off, but that he, Mr. Robertson and Mr. Wallace are in unanimous agreement that this should not be done. Instead, there have been discussions about the possibility of spinning off, either in whole or in part, those companies where growth is not developing as rapidly as it is throughout the remainder of the Corporation. In particular, he stated that such discussions had centered upon the Process Engineering Group, the Railroad and the Textile Group. In this connection, he pointed out that the Textile Group is a substantial contributor of cash even though it is not in a growth area. Mr. Salgo stated that the earnings of the Process Engineering Group are small and we need to seriously consider whether this group could be sold to another company. With respect to the Railroad, he stated that there is a question as to whether it should eventually go into a larger railroad system.

Mr. Salgo further stated that it would be very helpful if a committee from the Board of Directors could study the possible divestiture of the Bangor and Aroostook Railroad resulting in public ownership of it, either in whole or in part. He asked Mr. Curtis M. Hutchins to serve as Chairman and Messrs. George H. Seal and Robert G. Stone to serve as members of this Committee, with Mr. W. Jerome Strout as an ex-officio member and advisor to the Committee."

The minutes of the BPC board meeting of May 21, 1969 referred to the BAR as follows (Appendix 775-76):

"BANGOR AND AROOSTOOK RAILROAD.

Mr. Curtis M. Hutchins, as Chairman of a special committee appointed by Mr. Salgo at the Board of Directors meeting held April 1, 1969 (Reference: BPC-4-1-69-28), reported that he and Messrs. Robert G. Stone and George H. Seal (members of the special committee) have just completed a study of the situation with respect to the Bangor and Aroostook Railroad and wish to submit to the Board their unanimous report through Mr. Hutchins.

Mr. Hutchins stated that there appears to be three possibilities

sible sale to Amoskeag was discussed extensively. The board showed considerable interest in the sale at the time and gave the impression of strongly favoring it. These minutes, if not sufficient in themselves to lead a reasonable person to believe that the registration statement was misleading, certainly would have impelled a reasonable person

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which could be adopted with respect to the future of the Railroad. Bangor Punta might keep the Railroad as is, merge the Railroad with another railroad if that were possible, or sell the Railroad at the best possible price.

Mr. Hutchins stated that keeping the Railroad is not very appealing. He pointed out that because of the increased use of trucks and the restricted nature of the territory involved, it is doubtful that the traffic on the Railroad will increase. It appears that if the Railroad is to break even over the next five years, it will be necessary to spend substantial amounts of money for new freight cars and other equipment. He also stated that in discussing the situation with Mr. W. Jerome Strout, President of the Railroad, it appears that the amount of money to be expended might be as much as $5,000,000. Under these circumstances, Mr. Hutchins pointed out that it becomes more and more difficult to justify retention of the Railroad.

Mr. Hutchins next discussed the second possibility, that is, consolidating with another railroad. In this connection, he felt that a combination with the Boston & Maine Railroad, if otherwise possible, might result in Bangor Punta's receiving a third to a 40% interest in a new company. The consideration, however, would be in the form of securities rather than cash. Mr. Hutchins did not feel that this would be a palatable solution.

Mr. Hutchins next considered the question of selling the Railroad and to whom it might be sold. He pointed out that neither the Penn Central nor the Norfolk and Western Railroads have any known interest in the Bangor and Aroostook Railroad and a merger with either of these railroads is very unlikely. He stated that the only person whom he knew who might be interested in the Railroad is Mr. F. C. Dumaine, Jr., Chairman of Amoskeag Company. Mr. Hutchins stated that he has had preliminary discussions with Mr. Dumaine who had indicated that he might be willing to pay $5,000,000. in cash, a combination of cash and Bangor Punta securities, or Bangor Punta securities for the stock of the Bangor and Aroostook Railroad owned by the Corporation. At this point, Mr. Salgo asked whether it might be wise to offer to Mr. Dumaine 51% of the stock of the Bangor and Aroostook Railroad at book value, with an option to purchase the remaining 49% at a higher

to explore further. The only additional investigation by First Boston was to question company officials about the possible sale of the BAR. First Boston did not seek verification of the officials' answer that a sale was not anticipated at that time. Cf. *Escott* v. *Barchris*, 283 F.Supp. 643, 697 (S.D.N.Y. 1968, McLean, D.J.).[24] It did not make a more careful search of BPC's records, nor did it talk to officials

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price, with a total consideration, therefore, of approximately $7,000,000.

(At this point, Mr. Flick was called away from the meeting and Mr. Wallace acted as Secretary for the remainder of the meeting.)

Mr. Hutchins stated that, in his opinion, Mr. Dumaine would not agree to a price of $7,000,000., but that he probably would be able to obtain the approval of the Board of Directors of Amoskeag Company at a price of $5,000,000.

Mr. Hutchins stated that he is not asking for an approval by the Corporation's Board of Directors at this time, but only the authority to continue discussions with Mr. Dumaine. He stated that he wishes to first ascertain whether Amoskeag Company is willing to submit a definitive proposal.

Mr. Salgo next suggested that he would like to have Mr. Dumaine transfer to the Corporation 22,500 shares of Bangor Punta $1.25 Convertible Preference Stock as consideration for an option on 51% of the Railroad, the option to be for sixty days with the provision that the stock would be forfeited if the option is not exercised. In discussing Mr. Salgo's proposal, Mr. Strout pointed out that Mr. Dumaine also wishes to enter into an arrangement with the Maine Central Railroad; he does not believe the Maine Central Railroad will agree if such an agreement existed between Amoskeag Company and Bangor Punta Corporation.

After considerable discussion, it was the consensus of the Board that Mr. Hutchins should attempt to negotiate on the 49/51% basis suggested by Mr. Salgo, but that he has the authority to negotiate on the basis of a sale of 100% of the Bangor and Aroostook Railroad subject to further investigation of accounting and tax ramifications of such a transaction and approval by the Board of Directors or the Executive Committee of the Board of Directors."

24 The standard of reasonableness under §11 of the 1933 Act is that of "a prudent man in the management of his own property". 15 U.S.C. §77k(c)(1970). It is unnecessary for us to decide whether a reasonableness standard should be imposed under §14(e) since First Boston's conduct, in our view, went far beyond mere negligence.

at Amoskeag after it discovered from the minutes that Amoskeag was the likely buyer. Under these circumstances, First Boston's certification of the BPC registration statement carrying the BAR at $18.4 million amounted to an almost complete abdication of its responsibility to potential investors, to CCI, and to others who relied upon it to detect misrepresentations. We hold that First Boston possessed enough information reasonably to deduce that the BPC registration statement was materially inaccurate.

We hold that the conduct on the part of First Boston and its officers violated §14(e).[25]

(3) *Causation*

One of the fundamental issues upon which we disagree with the district court is that of causation.

The district court correctly pointed out that CCI neither bought nor sold Piper stock on the basis of the communications from the Piper management, the May 8 press release or the BPC registration statement. The court concluded that CCI was seeking damages as a "defeated contender for control" without showing that "a single exchanging Piper shareholder would have refrained from the exchange *and* taken an offer for his shares from Chris-Craft instead of that from Bangor Punta". 337 F.Supp. at 1139. (emphasis that of district court). We hold that the district court applied inappropriate causation principles and erred in assessing the nature of CCI's complaint.

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25 We agree with the district court that there is no merit to CCI's other claims against First Boston, essentially that it was the chief strategist for Piper and BPC in the control battle. The district court found, based on substantial evidence, that in its capacity as investment banker First Boston merely provided professional services to these companies. The business decisions that led to violations of the securities laws were initiated by these companies, not by First Boston in its role as investment banker. We are aware of no authority for holding First Boston liable in that capacity.

We agree with the district court's findings that CCI failed to show with reasonable certainty that it would have obtained a controlling position in Piper had it not been for the violations of the securities laws by BPC and First Boston. On the other hand, it is equally clear that BPC itself obtained control through its violations of the securities laws.

Since failure to disclose the BAR negotiations was a material omission, the next question is whether such omission was relied upon. It is important to note that, since the harmful effect of the negligence in this case did not depend upon the exercise of volition by CCI, but instead upon the exercise of volition by other persons, CCI need not show that it relied upon the deception. CCI must show that there was a misrepresentation upon which the target corporation stockholders relied and that this was in fact the cause of CCI's injury. See *Vine* v. *Beneficial Finance Co.*, 374 F.2d 627, 635 (2 Cir.), *cert. denied*, 389 U.S. 970 (1967).

We have held that reliance is established in a Rule 10b-5 action if the " 'misrepresentation is a substantial factor in determining the course of conduct which results in [the recipient's] loss' ". *List* v. *Fashion Park, Inc.*, 340 F.2d 457, 462 (2 Cir.), *cert. denied*, 382 U.S. 811 (1965). In many instances, courts have applied a subjective test to the reliance requirements, considering such factors as the plaintiff's general business expertise, *Clement A. Evans & Co.* v. *McAlpine*, 434 F.2d 100, 104 (5 Cir. 1970), his familiarity with the affairs of the corporation, *Kohler* v. *Kohler Co.*, 319 F.2d 634, 641-42 (7 Cir. 1963), and his access to the information misrepresented, *Hafner* v. *Forest Laboratories, Inc.*, 345 F.2d 167, 168 (2 Cir. 1965). See generally Note, *Reliance Under Rule 10b-5: Is the "Reasonable Investor" Reasonable?*, 72 Colum. L. Rev. 562 (1972).

Where the transaction is accomplished through impersonal dealings, such as on a stock exchange, or for some other reason the factors that influenced the parties are not readily apparent, the decisions have discussed liability in terms of the "materiality" of the misrepresentation. See *Heit* v. *Weitzen*, 402 F.2d 909, 913 (2 Cir. 1968), *cert. denied*, 395 U.S. 903 (1969); *List* v. *Fashion Park, Inc., supra*, 340 F.2d at 462-64; *Kahan* v. *Rosenstiel*, 424 F.2d 161, 173-74 (3 Cir. 1970). This constructive reliance principle is particularly appropriate in class actions where proof of actual reliance by numerous class members would be impracticable. *Kahan* v. *Rosenstiel, supra.*

The Supreme Court adopted this principle in *Mills* v. *Electric Auto-Lite Co.*, 396 U.S. 375 (1970). *Mills* was a class action brought by shareholders under §14(a) of the 1934 Act, 15 U.S.C. §78n(a) (1970), complaining that proxy solicitation material recommending a merger failed to disclose a conflict of interest. The proxy contest was won by the alleged wrongdoers and they needed the votes of minority shareholders to achieve the victory. The Court, in an opinion by Mr. Justice Harlan, stated the causation principle to be applied:

> "Where there has been a finding of materiality, a shareholder has made a sufficient showing of causal relationship between the violation and the injury for which he seeks redress if, as here, he proves that the proxy solicitation itself, rather than the particular defect in the solicitation materials, was an essential link in the accomplishment of the transaction." 396 U.S. at 385.

The Court established a presumption of reasonable reliance in order to avoid an overly difficult burden of proof. This was to encourage the vigorous enforcement of the securities laws through shareholder suits, and to effectuate the con-

gressional purpose of enabling shareholders to make informed decisions "by resolving doubts in favor of those the statute is designed to protect". *Id.*

The Supreme Court recently held that the *Mills* principle is applicable to a Rule 10b-5 damage action. *Affiliated Ute Citizens* v. *United States*, 406 U.S. 128 (1972). In *Ute*, members of a large class of security holders had been influenced to sell because of a failure to disclose. The Court held:

> "Under the circumstances of this case, involving primarily a failure to disclose, positive proof of reliance is not a prerequisite to recovery. All that is necessary is that the facts withheld be material in the sense that a reasonable investor might have considered them important in the making of this decision . . . . This obligation to disclose and this withholding of a material fact establish the requisite element of causation in fact." 406 U.S. at 153-54.

Accord, *Kohn* v. *American Metal Climax, Inc.*, 458 F.2d 255, 288-91 (3 Cir. 1972).

The district court below acknowledged that in "a proper case" the *Mills* test is sound, but concluded that this was not an appropriate case. It also held that §14(e) does not in any way alter the result. 337 F.Supp. 1139-40. We disagree.

The *Mills-Ute* test may be appropriately invoked, as here, in the context of a suit under §14(e) by an offeror against the target corporation and its allies. In such an action, the claim, as here, usually will be that the offeror's opponents have defeated him or impaired his efforts by misleading the target shareholders. *H.K. Porter Co.* v. *Nicholson File Co.*, *supra*, 4 CCH Fed.Sec.L.Rep. at 93,080-81. Concentration upon such shareholders often is the primary means of defeating the tender offer. Since the

offeror usually is a sophisticated businessman, his opponents rarely will be able to deceive him directly. As we said in *Crane Co.* v. *Westinghouse Air Brake Co.*, 419 F.2d 787, 796 (2 Cir. 1969), *cert. denied*, 400 U.S. 822 (1970):

> "When [the offeror] entered the securities market with its tender offer, it was entitled to the Act's protection not only against being deceived itself but also against deception of the investing public designed to prevent the public from entering into securities transactions." [26]

In the instant case, the offeror was not directly deceived but it was directly injured by defendants' deception of the Piper shareholders.

The fact that CCI was not directly deceived is what makes application of the *Mills-Ute* test appropriate and essential. It would be unduly burdensome to require an offeror to prove actual reliance when, as here, there are numerous shareholders who undoubtedly possess a wide range of expertise and knowledge. It would be impractical to require CCI to prove that each individual Piper shareholder who failed to trade for CCI's stock, or who traded for BPC's stock, relied upon defendants' misrepresentations in doing so. These impracticalities are avoided by establishing a presumption of reliance where it is logical to presume that reliance in fact existed. *Kohn* v. *American Metal Climax, Inc.*, *supra*, 458 F.2d at 288-91. As we have stated above, §14(e) was designed to protect offerors from

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26 In *Crane*, the offeror, Crane, made a tender offer for stock in Air Brake, but was thwarted when an ally of Air Brake, Standard, made heavy market purchases in Air Brake so as to manipulate its price. We held that Crane was entitled to specified relief under Rule 10b-5 even though it had not established that its tender offer would have been more generally accepted if these violations had not been committed. The district court in the instant case distinguished Crane as a decision where the "character of the violation and the clear causal nexus were crucial to the . . . result". 337 F.Supp. at 1140. We do not read *Crane* in such a restricted fashion.

unfair and unlawful opposition. By "resolving doubts in favor of those the statute is designed to protect", *Mills* v. *Electric Auto-Lite Co., supra*, 396 U.S. at 385, we are implementing congressional intent not only to protect investors, but to make sure that contests for control between offerors and incumbent management, or other offerors, shall proceed fairly.

In applying the *Mills-Ute* test to the instant action, we presume that the Piper shareholders would not have accepted the BPC exchange offer but for the misrepresentations to which we have referred above. Even if we assume arguendo that BPC's offer was superior to that of CCI, taking into account the BAR loss, we still must conclude that BPC's success was unlawfully attained. Piper shareholders had a third option, i.e. to hold their shares, which presumably they would have chosen if all the material facts had been disclosed. Under the *Mills-Ute* test, we must presume that BPC's offer was not so appealing, considering the BAR loss, as to have attracted any takers. See *Vine* v. *Beneficial Finance Co., supra*, 374 F.2d at 635. Since BPC eventually acquired only about 51% of the outstanding Piper shares, it is clear that the 7% acquired through its exchange offer was critical to its success. Reliance and causation have been shown.

What the securities law violations caused was a denial to CCI of a fair opportunity to compete for control of Piper. The specific injury sustained was a reduction in the value of CCI's Piper holdings upon BPC's unfairly obtaining control. CCI spent large sums of money in actively seeking control. Its purchases were made in the reasonable belief that its opponents would battle hard but within the law. CCI is entitled to compensatory damages for the decline in the value of the minority shareholder's interest with which it became encumbered as a result of competing against those who violated the securities laws.

Even if CCI had discovered, prior to purchasing some of the shares that it now holds, that BPC was competing unfairly, it was not required to mitigate damages by dropping out of the contest. A victim of a securities fraud does not have to elect between pursuing his goal in spite of the unlawful tactics of his opponents and recovery of damages for injuries sustained. Indeed, if CCI's persistence in the fight despite the violations had brought it victory, it would not have sustained damages from being put in a minority shareholder's position.

The Piper family's violations also caused injury to CCI. Piper contends that since CCI was not able and willing to accept any more shares than it did accept as a result of the cash tender offer, the January letters to shareholders and the Grumman press release were harmless. The evidence does not support this contention.

Since CCI had decided by the time of the cash tender offer that its objective was to win control of Piper, it clearly was willing to accept as many shares as it could obtain. While it was ready to commit itself to purchase only 300,000 shares, that limitation does not indicate that it would not accept a substantial number of additional shares if tendered.[27] Indeed, it expressly reserved the right to purchase more than the 300,000 shares.[27a] And although Piper offered some evidence indicating that CCI might have trouble

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27 Mr. Gordon testified, when asked why CCI had committed itself to purchase no more than 300,000 shares, that one reason was that "[w]e did not want . . . Piper to emphasize the fact that the financing for the shares beyond 300,000 had not yet been arranged—to emphasize that successfully, because we knew we could arrange it, but we didn't have it at that time."

27a Officers of CCI announced to the press that the tender offer was successful. The Piper family would have us construe this announcement as a concession that CCI did not expect or desire more from its cash tender offer. As is well known, such statements in this context often are made for the sake of appearance. We decline to ascribe to them the interpretation suggested by the Piper family.

financing additional purchases, it appears that such financing was available. Mr. Gordon testified that, before the cash tender offer had expired, he had arranged with Burnham & Co. to borrow up to $22,000,000 if needed to purchase shares in excess of 300,000. Moreover, the fact that CCI bought only a few shares of Piper on the market after the termination of its cash tender offer is of little probative value. There are many possible explanations for this consistent with CCI's position that it would have purchased additional shares pursuant to the cash tender offer. For example, CCI might have been avoiding the expense of searching out small blocks of shares and the high transactional costs involved in purchasing them. We are satisfied that CCI had a desire to purchase, and was capable of purchasing, a substantial number of additional shares pursuant to its tender offer.

The January letters to shareholders and the Grumman press release misled the Piper shareholders into believing that CCI's tender offer was undesirable. CCI's tender offer could be fruitful only if Piper shareholders believed that the price was currently a fair one and would remain so for at least a reasonable period in the future. The fairness of the offer is demonstrated by the fact that, despite the misrepresentations of the Piper family, over 300,000 shares were tendered. Considering the soundness of the offer and the materiality of the Piper family's deceptions, it is a reasonable presumption that CCI was unlawfully denied the opportunity to purchase additional shares. See *Crane Co. v. Westinghouse Air Brake Co., supra*, 419 F.2d at 797. Moreover, these misleading statements most likely had a continuing adverse effect on CCI's attempts to acquire Piper shares. When Piper shareholders were deciding whether or not to accept CCI's exchange offer, many undoubtedly remembered and were influenced by the Piper

family's misleading January statements portraying CCI as a company that made inadequate and unfair offers.

We hold that, considering the narrow margin of victory here, the Piper family's misstatements and omissions in the January shareholder letters and the Grumman press release denied to CCI a fair opportunity to win the contest for control.

The June and July letters to Piper shareholders are a different matter. Although they omitted any reference to the arrangement between the Piper family and BPC whereby the family might gain a considerable amount of money if BPC were to be successful in gaining control of Piper, CCI protected itself against injury from such omission by sending letters to all Piper shareholders on June 16 exposing this non-disclosure by the Piper family. The nature of the Piper family's personal stake in the exchange offer was fully described. We therefore conclude that this omission was rendered harmless.

We hold that the record establishes that the injuries sustained by CCI were caused by the violations of the securities laws by BPC and its named officers, First Boston and its named officers and members of the Piper family.

(C) Violations of Rule 10b-6 Under 1934 Act

We turn now to CCI's claim that BPC's cash purchases between May 14 and 23 of three large blocks of Piper stock violated Rule 10b-6 under the 1934 Act, 17 C.F.R. §240.10b-6 (1972), and that such purchases caused injury to CCI. We hold that they did.

Rule 10b-6 prohibits bids for or purchases of a security by or on behalf of the issuer of a security if the security is "the subject of . . . [a] distribution". Included within the prohibition are bids for or purchases of "any right to purchase any such security". Clearly here, Piper stock, within the meaning of Rule 10b-6, was a "right to purchase" BPC stock.

On May 14, BPC purchased 78,600 Piper shares from Fund of Funds Proprietary Fund, Ltd. (FOF). On May 15, it purchased an additional 20,000 Piper shares from American Securities Corporation. And between May 16 and 23, it purchased an additional 21,600 Piper shares from Bay Securities Corporation. Thus, during this 10 day period and while its exchange offer for Piper shares was pending, BPC made three block purchases of Piper stock totalling 120,200 shares.

In our earlier en banc decision, we held that these purchases fell within the prohibition of the first sentence of Rule 10b-6. *Chris-Craft Industries, Inc.* v. *Bangor Punta Corp.*, 426 F.2d 569, 576-77 (2 Cir. 1970). Our reasoning was that such large purchases by BPC had a tendency to boost the market value of Piper stock to an artificial level. Since the purchases were made shortly after BPC announced on May 8 that it would make an exchange offer, reasonable investors were likely to have attributed the increase in the price of Piper stock to the soundness of BPC's exchange offer. As a result, the operation of the market would tend to raise the market price of the BPC package to align it with the inflated Piper price. Rule 10b-6 was designed to prevent such manipulation of a security which is "the subject of . . . [a] distribution". See *SEC* v. *Scott Taylor & Co.*, 183 F.Supp. 904, 907 (S.D.N.Y. 1959). We therefore concluded that Rule 10b-6 had been violated but we remanded for a determination of whether the exemption contained in Rule 10b-6(a)(3)(2) was applicable and what remedy, if any, was appropriate. 426 F.2d at 577.

On remand, BPC claimed the applicability of the exemption only with respect to its purchase from FOF on May 14. The district court held that "[a] literal reading of the exemption requires a finding that the [FOF] purchase,

like the others, was not exempted". 337 F.Supp. at 1141. BPC does not contest this holding. The court concluded, however, that these were "technical violation[s]" and that there was not enough substance to them to support a finding that CCI was damaged. *Id.* at 1141-43. We disagree.

Since the violations constituted a manipulation of the price of BPC, the question arises whether CCI is a proper party to sue on this claim since it did not accept the BPC exchange offer.[28] CCI's contention is not that it was misled by BPC's purchases of Piper stock. It does contend that Piper shareholders were misled into accepting the BPC exchange offer because the Rule 10b-6 violations had a tendency to inflate the market value, and that CCI, as BPC's rival for the Piper stock, was thereby injured. Cf. *Vine* v. *Beneficial Finance Co.*, 374 F.2d 627, 635 (2 Cir.), *cert. denied*, 389 U.S. 970 (1967). The SEC's policy statement of May 5 announced that purchases of stock of a target company during the pendency of an exchange offer are forbidden by Rule 10b-6 in order to promote fairness in contests for control. We find nothing in the language or history of Rule 10b-6 to suggest that only purchasers of the manipulated stock are entitled to bring an action.[29] We hold that CCI has a right of action to complain that BPC's Rule 10b-6 violation caused it injury.

The remaining question is whether BPC's cash purchases misled the Piper shareholders by artificially boosting the market value of the BPC securities and, if so, whether this deception was in fact the cause of the injury for which CCI seeks redress. The district court held that, although the

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28 The district court held that CCI had standing to sue on the Rule 10b-6 violation. 337 F.Supp. at 1133.

29 Rule 10b-6 does not contain the clause, "in connection with the purchase or sale of any security", which limits a cause of action under Rule 10b-5. *Birnbaum* v. *Newport Steel Corp.*, 193 F.2d 461 (2 Cir.), *cert. denied*, 343 U.S. 956 (1952).

purchases were literally proscribed by Rule 10b-6, Piper shareholders were not necessarily misled because, among other reasons, the purchases were not designed to produce a stimulating effect, were not radiated into the general market, and were not made through an exchange or regular broker-dealer. 337 F.Supp. at 1142-43. We hold that, since the purchases were in violation of Rule 10b-6 and were not exempt, CCI is entitled to recover damages from BPC based on such violations.

Either the purchases were prohibited by the Rule or they were not. If they were, as we have held, then presumptively a stimulating effect was produced which misled the public. Rule 10b-6 was drafted by the SEC on the basis of its considerable expertise and familiarity with market factors. It determined that a purchase that meets all the criteria set forth in the Rule will have a false prodding effect on the price of the distributed security and therefore should be outlawed. On the basis of the facts presented here, we refuse to second guess the wisdom and rationale of the Rule. Cf. *H. Kook & Co.* v. *Scheinman, Hochstin & Trotta, Inc.*, 414 F.2d 93, 98 (2 Cir. 1969). Piper shareholders presumptively were deceived by a material alteration in the value of the exchange package. They no doubt were influenced by this deception to take advantage of what seemed to be a highly favorable BPC exchange offer.[30]

BPC's unlawful conduct denied CCI a fair chance to compete for control of Piper. We cannot say that CCI would have obtained a majority of Piper stock had BPC not violated the law, but it is a fact that BPC obtained control through its unlawful acts. Its May purchases of large

30 CCI need not prove actual reliance by Piper shareholders. Rule 10b-6 creates a presumption that illegal purchases will substantially inflate the price of the security. A reasonable investor is likely to rely on this inflation in deciding to accept the exchange offer. See *Mills* v. *Electric Auto-Lite Co.*, *supra*, 396 U.S. at 385; *Affiliated Ute Citizens* v. *United States*, *supra*, 406 U.S. at 153-54.

blocks of Piper stock operated in the market to make BPC's exchange offer deceptively attractive. Success on that offer was necessary to achieve control. More important, the unlawful purchases themselves constituted about 7% of the outstanding shares of Piper. BPC eventually acquired only 51%. Even arithmetically, it is apparent that the block purchases in violation of Rule 10b-6 were essential to achieve control. BPC's attainment of a majority position has caused CCI to suffer a decline in the value of its Piper holdings.

We hold that CCI is entitled to recover damages from BPC based on its violations of Rule 10b-6.

(D) Relief To Be Granted For Violations of Section 14(e) and Rule 10b-6

Having held that all defendants violated Section 14(e) and that BPC violated Rule 10b-6, we turn now to the form of relief to which CCI is entitled.

Normally, the form of appropriate relief should be left for determination by the district court upon remand, as was done after consummation of mergers achieved as a result of securities laws violations in *Mills* v. *Electric Auto-Lite Co.*, 396 U.S. 375, 386-89 (1970); *J. I. Case Co.* v. *Borak*, 377 U.S. 426, 433-35 (1964); *Crane Co.* v. *Westinghouse Air Brake Co.*, 419 F.2d 787, 803-04 (2 Cir. 1969), *cert. denied*, 400 U.S. 822 (1970).

In the instant case, however, we believe that it is incumbent upon us to provide specific guidance to the district court as to the form of relief to be granted upon remand. There are several reasons for this. First, as indicated above, the district court did not reach the issue of relief to be granted, since it held that most of the alleged securities laws violations had not been proven, that those proven had not caused injury to CCI and that CCI had failed to prove its claim for damages. Second, under the

posture of the case in the district court, CCI limited its claim for relief to damages, but on appeal has pressed its claim for equitable relief as well as damages. Third, this litigation has been under way for more than three years, with one appeal already having been decided en banc by our Court. And, finally, certain of the questions presented are of first impression, chiefly the application of the anti-fraud provisions of the federal securities laws to a contest for acquisition of a controlling stock interest in a target corporation.

In short, the district court deserves guidance from this Court on the form of relief to be granted. We therefore order, upon remand and after appropriate opportunity has been afforded to the parties to be heard on the issue of relief, that the district court should grant at least the following relief:

(1) *Damages*

Piper has come under the dominance of BPC, with many of its management positions being assumed by BPC officers. It has been operated that way for two or three years. Divestiture of the ill-gotten shares would not be appropriate under the circumstances of this case because it would be difficult to administer and would unnecessarily reopen the control battle. CCI understandably no longer desires to take control of a company that has been substantially changed. It seeks damages.

We have held that the unlawful conduct of the Piper family,[31] of BPC and its named officers, and of First Boston

31 The Piper Aircraft Corporation itself was not a perpetrator of the violations of the securities laws. The evidence shows that members of the Piper family acted not on behalf of the corporation in committing their illegal acts, but in their own individual interests. The district court correctly characterized Piper as "the prize in the battle, not a contender". 337 F.Supp. at 1146. We agree that no liability is to be imposed on the Piper Aircraft Corporation.

and its named officers has caused financial loss to CCI for which it should be compensated. The measure of damages should be the reduction in the appraisal value of CCI's Piper holdings attributable to BPC's taking a majority position and reducing CCI to a minority position, and thus being able to compel a merger at any time. Since the conduct of each of the defendants, through their violations of the securities laws, contributed to the success of BPC's takeover attempt, a judgment should be entered assessing damages against all defendants jointly and severally. See Section 18(b) of the Securities Exchange Act of 1934, 15 U.S.C. §78r(b) (1970).

(2) *Equitable Relief*

We further hold that BPC should be denied the fruits of obtaining Piper shares illegally. We therefore direct that the district court include in its judgment an injunctive provision barring BPC from voting for a period of at least 5 years the Piper shares it obtained through the unlawful May cash purchases and those it obtained through its exchange offer.[32]

While we believe that the foregoing relief should be sufficient, our direction that the two provisions indicated above should be included in the judgment to be entered on remand is not intended to foreclose the district court from fashioning such additional appropriate relief as it may find necessary to implement our decision herein, after affording the parties an opportunity to be heard on the issue of relief.

The judgment of the district court on the appeal in No. 72-1064 is reversed and the case is remanded.

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32 This injunctive provision of course would not apply to those Piper shares which are retransferred to former Piper shareholders who take advantage of the rescission order referred to below.

III.

BANGOR PUNTA CORPORATION v. CHRIS-CRAFT INDUSTRIES, INC. (NO. 72-1120)

In this second of three related appeals, BPC appeals from the district court's dismissal after trial, 337 F.Supp. 1147 (S.D.N.Y. 1971), of BPC's complaint which sought damages from CCI for alleged violations of the securities laws during the contest for control of Piper, BPC's principal claim being that, because of CCI's wrongful acts, BPC paid more than it otherwise would have paid to acquire control of Piper.

The complaint alleged violations of various provisions of the securities laws, including violations of Sections 9(a)(2) and 10(b) of the 1934 Act, 15 U.S.C. §§78i(a) and 78j(b) (1970); of Rules 10b-5 and 10b-6 promulgated under the 1934 Act, 17 C.F.R. §§240.10b-5 and 240.10b-6 (1972); and of Section 17(a) of the Investment Company Act of 1940, 15 U.S.C. §80a-17(a) (1970).

At the trial before Judge Pollack, BPC adduced no proof specifically as plaintiff in the instant case, but instead relied on the record in *Chris-Craft Industries, Inc.* v. *Piper Aircraft Corporation, et al.* (No. 72-1064). After trial, the district court dismissed the complaint essentially on the grounds that the winner in a contest for control is not entitled to seek damages against the loser for alleged violations of the securities laws, that whatever BPC paid for control was attributable not to any alleged securities law violations by CCI but to BPC's own determination to obtain control, and that BPC had not supported with credible evidence its contentions that CCI had violated the securities laws or that such violations had caused injury to BPC.

Since we affirm the district court's dismissal of the complaint on the ground that BPC failed to adduce sufficient evidence to prove that the securities laws were violated, we do not reach the question whether BPC's allegations state a claim for relief under Rule 10b-5.

(A) Claim of Manipulation of Prices of CCI Stock

The gravamen of BPC's claim is that CCI violated the securities laws in an attempt to gain control of Piper, and that these violations caused BPC to pay more for Piper stock than it otherwise would have been required to pay. BPC's prime contention is that CCI acted in concert with others unlawfully to inflate the market price of CCI stock at the time of CCI's exchange offer so that the offer would be deceptively attractive. This alleged inflation of CCI's price is said to have had the secondary effect of driving up the price of Piper stock.

To prove such price manipulation, BPC relies upon inferences from a series of events. The relevant occurrences began in 1968 when Roger Spencer, a vice-president of Mitchell, Hutchins & Co., Inc. (a brokerage firm with close ties to several mutual funds), took an interest in CCI as a possible investment for Mitchell, Hutchins' clients. Spencer conducted an investigation of CCI that included several conversations with Herbert Siegel, President of CCI. Spencer subsequently recommended to several of his clients that CCI would be a sound investment. Several of these funds—Technology Fund, Inc. (Tech Fund), Investors Diversified Services, Inc. (IDS), Newton Fund, Inc. and Commonwealth Edison Pension Fund, Inc.—eventually were involved in the purchase of CCI stock.

IDS is a manager of a complex of mutual funds. Two of its managed funds, Investors Mutual, Inc. and Investors Stock, Inc., purchased 28,300 shares of ICC common in the period January 14-23, 1969. Another purchase of 53,900

shares was made on January 24 and 25. By January 31, the two funds had acquired 94,600 common and 24,700 of $1.40 preferred; another IDS fund had purchased 9000 common.

Tech Fund, a registered investment company, not only purchased many shares of CCI stock, but also, as discussed above in our opinion in No. 72-1064, sold 101,100 shares of Piper to CCI on January 22 at $65 per share. On the same day that the Piper sale was completed, Tech Fund apparently decided to acquire 50,000 shares of CCI common and 10,000 shares of CCI preferred. These purchases were made between January 23 and February 25.

About this time, several other organizations also began making purchases of CCI stock in large amounts. American Investors Fund, Inc. (AIF) bought 22,500 common and $78,000 of 6% convertible debentures on four trading days beginning February 7. Keystone Custodian Services, Inc. (Keystone), fund managers, recommended that its Polaris and S-4 Funds buy CCI stock. The two funds purchased 130,000 shares of CCI common between January 20 and April 28. Between January 14 and February 25, these four organizations acquired 17% of CCI's outstanding common stock. These large purchases significantly contributed to a rise in the price of CCI common from 40 on January 13 to 58¼ on February 11, an increase of 45% over the average price during the preceding six weeks.

BPC maintains that these heavy market purchases by the funds were instigated by CCI through agreements and by providing inside information abouts its bids for Piper. Mitchell, Hutchins allegedly was the intermediary in this scheme. BPC's evidence of "agreements" clearly is insufficient. It contends that Tech Fund agreed to purchase CCI stock in return for CCI's buying Tech Fund's Piper holdings at a "premium price". This is pure surmise. There is no evidence of an actual agreement to that effect or that

the parties even discussed such an agreement. The price paid for the Piper stock, $65, was not a "premium" price since the next day CCI announced a large cash tender offer at the same price. IDS allegedly made purchases because it was a principal holder of CCI senior notes and therefore had an interest in the success of CCI's takeover attempt. This interest is not sufficient proof that IDS wilfully manipulated the price of CCI stock.

BPC also has failed to show that CCI gave illegal insider tips to spur market purchases of its stock. CCI did make known that it was planning to make acquisitions in the leisure-time field but this was a well publicized intention.[33] Indeed, most of the funds' purchases were made after CCI announced its tender offer. Any well informed investor by then would have known CCI's plans. It is evident that the funds purchased CCI heavily because their customary sources of information, such as Mitchell, Hutchins, revealed that CCI's acquisition of a company such as Piper probably would increase the value of CCI stock. It was a reasonable investment decision on their part, induced not by a desire to inflate artificially the value of CCI stock but by the prospect of gain. As we indicate below, these investments proved to be ill-advised and of little benefit to CCI or the funds. We cannot conclude on the basis of such evidence that the district court's findings were clearly erroneous.

BPC further contends that a manipulative intent is shown by the timing of the funds in disposing of their CCI holdings. CCI stock decreased in value substantially in the spring and summer of 1969, along with the general market decline. One of the three IDS funds sold its entire

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33 As we stated above in our opinion in No. 72-1064, CCI had sought financing in late 1968 by selling $26 million in debentures for the express purpose of making acquisitions in the leisure-time field. CCI also had made substantial investments in Warner Bros. and Harley-Davidson before purchasing Piper shares.

9000 shares in March because of CCI's difficulties with the Piper takeover. The other two IDS funds retained their CCI investments and sustained book losses of more than $4,600,000. Tech Fund, after selling 1600 of its shares on March 28, decided on April 1 to sell out its entire position. It accomplished this total disposal by selling gradually through July 7. It sustained a $691,000 loss on an investment of $3 million. AIF sold out completely between April 30 and May 20. The Keystone funds retained their holdings until August 1 and disposed of their entire position within the month, incurring a $3,625,048 loss on a $6,447,579 investment. These funds sustained a total loss of about $9,000,000 on their investments in CCI.

BPC argues that the funds did not immediately dispose of their CCI stock in a declining market because they intended to keep CCI's stock prices at an unlawfully inflated level. There is no discernible pattern in the sales that supports such a conclusion. It may be that one of the considerations which influenced the decisions of these investors was concern for the success of CCI's exchange offer. But, even if so, the record does not establish that it was the sole or even dominant consideration. It is apparent that each investor took the course of action that it believed would minimize its losses. Some were erroneously optimistic and anticipated that CCI would be successful in its quest for control of Piper. But most sold out early. A major portion of the shares was sold before and during the CCI exchange offer, thus impairing rather than promoting its success. We conclude that the district court was not clearly erroneous in refusing to find either a scheme to boost the price of CCI stock or a purpose on the part of CCI and the funds to manipulate the market in CCI shares.

Moreover, the facts as found by the district court, which are based on substantial evidence, do not establish that an unlawful market manipulation occurred. BPC's reliance

upon *Crane Co.* v. *Westinghouse Air Brake Co.*, 419 F.2d 787 (2 Cir. 1969), *cert. denied*, 400 U.S. 822 (1970), is misplaced. There, Crane sought to take over Air Brake by a cash tender offer. Air Brake enlisted the aid of Standard to oppose the takeover. One of the means selected by Standard to achieve this objective was manipulation of Air Brake stock. On the last effective date of the tender offer, Standard, through a series of transactions, purchased on the market an extremely large number of shares at a price above the then market price, while at the same time secretly arranging for others to purchase at a much lower price many of the shares it had acquired. It was manifest from the secret deals and the intentional loss taken by Standard that it deliberately manenvered the market price of Air Brake stock in order to defeat Crane's tender offer.

In the instant case, unlike *Crane*, the requisite purpose and wilfullness for a market manipulation claim cannot be inferred from the established facts. BPC places unwarranted reliance on circumstantial evidence. The funds bought CCI shares because they believed that it was a wise investment. The securities laws do not proscribe all buying or selling which tends to raise or lower the price of a security. The securities laws are designed to create "investors markets where prices may be established by the free and honest balancing of investment demand with investment supply." H.R. Rep. No. 1383, 73 Cong., 2d Sess. 11 (1934). So long as the investor's motive in buying or selling a security is not to create an artificial demand for, or supply of, the security, illegal market manipulation is not established. See Section 9(a)(2) of the 1934 Act, 15 U.S.C. §78i(a)(1970).

We hold that BPC failed to prove that the funds acted from improper motive, that CCI encouraged them to do so or that unlawful market manipulation in fact occurred.

(B) Claim of Illegal Warehousing

BPC claims that, at the direction of CCI, Tech Fund instructed its affiliates to purchase and illegally "warehouse" Piper stock which these affiliates later tendered to CCI.

BPC bases this claim on the following facts. After CCI announced its exchange offer, it continued to purchase Piper shares on the market. On April 7, the SEC warned CCI that these purchases violated Rule 10b-6. CCI heeded this warning and ceased making purchases. On April 17 and 18, Tech Fund ordered two of its affiliates to start buying Piper stock. They acquired 14,700 shares by April 25. Of this total, 9,900 shares were tendered on June 5 to CCI pursuant to its exchange offer.

BPC argues that Tech Fund purchased these securities at the encouragement of Spencer of Mitchell, Hutchins, who supposedly acted under instructions from CCI. Tech Fund evidently did purchase the stocks because it hoped to take advantage of a favorable CCI exchange offer. Tech Fund also apparently relied at least in part upon the representations of Spencer. The record, however, does not support BPC's assertion that CCI arranged this purchase by Tech Fund or that it made promises of value to Tech Fund with regard to its exchange offer.

We hold that the district court was not clearly erroneous in rejecting BPC's claim of illegal warehousing.

We have considered BPC's other claims on this appeal, such as CCI's alleged violation of Section 17(a)(2) of the Investment Company Act of 1940, 15 U.S.C. §80a-17(a)(2)(1970), and have concluded that they are without merit.

The judgment of the district court on the appeal in No. 72-1120 is affirmed.

IV.

SEC v. BANGOR PUNTA CORPORATION (NOS. 72-1053 and 72-1140)

These are cross-appeals from a judgment entered November 17, 1971 after trial on the merits. 331 F.Supp. 1154 (S.D.N.Y. 1971). The SEC appeals from those provisions of the judgment which denied a permanent injunction against further violations of the securities laws and which imposed a condition upon BPC's rescission offer to former Piper shareholders. BPC cross-appeals from those provisions of the judgment which found BPC to have violated the securities laws and which ordered BPC to offer rescission to former Piper shareholders.

The SEC brought this action pursuant to Sections 20(b) and 22(a) of the 1933 Act, 15 U.S.C. §§77t(b) and 77v(a) (1970), and Sections 21(e) and 27 of the 1934 Act, 15 U.S.C. §§78u(e) and 78aa (1970). The complaint alleged that BPC's registration statement and prospectus for its Piper exchange offer violated the registration statement and prospectus requirement provisions of Sections 7 and 10(a) of the 1933 Act, 15 U.S.C. §§77g and 77j(a) (1970); and the antifraud provisions of both acts, Section 17(a) of the 1933 Act. 15 U.S.C. §77q(a) (1970), Section 10(b) of the 1934 Act, 15 U.S.C. §78j(b) (1970), and Rule 10b-5 promulgated under the 1934 Act, 17 C.F.R. §240.10b-5 (1972).

After trial of this action at the same time as the other two actions (the subject of the appeals in Nos. 72-1064 and 72-1120), the district court concluded that BPC had violated the securities laws, including the antifraud provisions of the 1933 and 1934 Acts. The court ordered that BPC offer rescission to all former Piper shareholders who had accepted BPC's exchange offer, subject to a condition which we shall discuss below. The court denied the SEC's

request that BPC be permanently enjoined from further violations of the securities laws.

On the SEC's appeal, to the extent the judgment is appealed from, we affirm in part, and reverse and remand in part. On BPC's cross-appeal, we affirm.

(A) Injunctive Relief

The district court concluded that, although BPC had violated the securities laws in disseminating a materially misleading registration statement and prospectus for a securities exchange offer, nevertheless "the Commission has failed to carry its burden to establish, with persuasive evidence, that Bangor-Punta, its officers, directors and employees have *a propensity or natural inclination* to violate the securities law." (emphasis added.) Accordingly, the court denied a permanent injunction against further violations. 331 F.Supp. at 1163. I disagree.[34]

Based upon the SEC's stautory responsibility under the 1933 and 1934 Acts[35] to seek a permanent injunction "[w]henever it shall appear to the Commission that any person is engaged or about to engage in any acts or practices which constitute or will constitute a violation" of the provisions of such Acts or any rule or regulation promulgated thereunder, I believe that the district court erred in denying a permanent injunction and I emphatically dissent from the opinion of Judge Gurfein affirming the denial of

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34 On this issue—the district court's denial of injunctive relief in the SEC's enforcement action—I would reverse the district court and remand with directions that it issue an injunction against further violations of the securities laws by Bangor Punta, its officers, directors and employees. But my opinion on this issue, I regret to say, has emerged as the minority view. The majority view is set forth in Judge Gurfein's separate opinion at pages 4991, 4966 *infra*.

35 Section 20(b) of the 1933 Act, 15 U.S.C. §77t(b) (1970); Section 21(e) of the 1934 Act, 15 U.S.C. §78u(e) (1970).

such injunction. The grounds of my dissent are as follows.[36]

(1) *Erroneous Standard*

First, the district court applied an erroneous standard in determining whether a permanent injunction should issue. The court held, as stated above, that the SEC had failed to show that "Bangor Punta, its officers, directors and employees have *a propensity or natural inclination* to violate the securities law." (emphasis added). It uniformly has been held that the correct standard is "whether there

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36 As to one finding of the district court with respect to which the SEC challenges the denial of an injunction, although the issue is a very close one, I am inclined to agree with my colleagues that the district court's finding of fact should not be set aside as clearly erroneous. Fed. R. Civ. P. 52(a); *Heyman* v. *A. R. Winarick, Inc.*, 325 F.2d 584, 589 (2 Cir. 1963).

The SEC contends that the court erred in refusing to find that BPC had decided by the early summer of 1969 to sell its BAR holdings to Amoskeag for $5 million and chose deliberately to postpone effectuating the sale in order to avoid recording and disclosing a loss of $13 million. Upon reviewing the entire evidence with respect to this aspect of the matter, however, I agree that we are not "left with the definite and firm conviction that a mistake has been committed." *United States* v. *United States Gypsum Co.*, 333 U.S. 364, 395 (1948). The SEC relies heavily upon the testimony of Dumaine to establish that a deal had been made prior to the close of the Piper exchange offer. The district court, which observed the demeanor of the witness, concluded that his testimony was not worthy of belief. On such a determination, I agree that we should not substitute our views for those of the trial judge who heard and saw the witness. Nor do I believe that we should find unreasonable the court's inferences drawn from undisputed evidence that BPC's delay in consummating the deal resulted from a prudent business decision to ascertain, through a complete investigation of legal and accounting ramifications before closing the deal, the precise impact of the sale.

Since the issue on this point is very close, I could well be wrong and the SEC may be correct in urging that the district court's finding was clearly erroneous. Nevertheless, for the reasons stated above, I prefer to resolve any doubt on this point in favor of the correctness of the district court's finding—especially in view of the more persuasive reasons set forth below which in my opinion demand reversal of the district court's denial of an injunction.

is a reasonable likelihood that the wrong will be repeated". *SEC* v. *Manor Nursing Centers, Inc.*, 458 F.2d 1082, 1100 (2 Cir. 1972).[37] See *United States* v. *W. T. Grant Co.*, 345 U.S. 629, 633 (1953); *SEC* v. *Culpepper*, 270 F.2d 241, 249 (2 Cir. 1959). There is a meaningful difference between the standards of "propensity or natural inclination to violate" and "reasonable likelihood that the wrong will be repeated". The district court's failure to perceive this difference and my colleagues' sanctioning the application of an erroneous standard cuts to the core of the error committed. This leads to the second ground of my dissent.

(2) *Requirement of Intent*

Second, in sanctioning a standard of "propensity or natural inclination to violate the securities laws", my colleagues have engrafted upon the standard required for an injunction in an SEC enforcement action a requirement not

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37 In *SEC* v. *Manor Nursing Centers, Inc., supra*, we expressly *rejected* appellants' contention that "the SEC must show more than a reasonable likelihood of future violations. . . . [A]ppellants must be shown to have a propensity or natural inclination to violate the securities laws." 458 F.2d at 1101.

In *Manor Nursing*, referring to the district court's opinion below in the instant case, we assumed that "it was not purporting to apply a new standard for the issuance of an injunction" in view of the court's reliance upon our decision in *SEC* v. *Texas Gulf Sulphur Co.*, 446 F.2d 1301 (2 Cir.), *cert. denied*, 404 U.S. 1005 (1971). 458 F.2d at 1101.

Since the author of the present opinion also was the author of *Manor Nursing*, I can state unequivocally that the *Manor Nursing* court was totally unfamiliar with the record in the instant case, other than the district court's opinion reported at 331 F.Supp. 1154; and of course, as with Judge Pollack when he denied the permanent injunction in the instant case, we did not know at the time of our decision in *Manor Nursing* that the conduct of Bangor Punta here ultimately would be held, as we now hold, to constitute serious violations of the antifraud provisions of the federal securities laws—including such conduct as recklessly failing to disclose in its registration statement and prospectus the true value of the BAR: hardly a minor omission, but a $13 million one.

required by Congress, by the Supreme Court or by our Court (prior to today's decision), namely, a *purposeful* violation of the securities laws and a showing of *intent*. In Judge Gurfein's words (p. 4994 *infra*), "In the last analysis we are dealing with *intent* . . . ." (emphasis added). I disagree.

To impose upon the SEC the burden of showing evil motive or intent to violate the securities laws as a condition to obtaining an injunction against further violations would be tantamount to converting a civil injunction enforcement proceeding into a criminal prosecution. As the Supreme Court said in reversing our Court in *SEC* v. *Capital Gains Research Bureau, Inc.*, 375 U.S. 180 (1963):[38]

> "This, of course, is but another way of putting the rejected argument that the elements of technical common-law fraud—particularly intent—must be established before an injunction requiring disclosure may be ordered. It is the practice itself, however, with its potential for abuse, which 'operates as a fraud or deceit' within the meaning of the Act when relevant information is suppressed. . . . Failure to disclose material facts must be deemed fraud or deceit within its intended meaning, for, as the experience of the 1920's and 1930's amply reveals, the darkness and ignorance of commercial secrecy are the conditions upon which

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38 *Capital Gains* involved the showing the SEC was required to make in order to obtain an injunction compelling disclosure under the Investment Advisers Act of 1940. The Court held that "Congress, in empowering the courts to enjoin any practice which operates 'as a fraud or deceit' . . . did not intend to require proof of intent to injure . . . . Congress intended [the Act] to be construed like other securities legislation 'enacted for the purpose of avoiding frauds,' not technically and restrictively, but flexibly to effectuate its remedial purposes." 375 U.S. at 195.

This applies a fortiori to the remedial injunctive provisions of the 1933 and 1934 Acts pursuant to which the SEC brought the instant injunction action. See note 35 *supra*.

> predatory practices best thrive. To impose upon the Securities and Exchange Commission the burden of showing deliberate dishonesty as a condition precedent to protecting investors through the prophylaxis of disclosure would effectively nullify the protective purposes of the statute." 375 U.S. at 200.

The absence of any such requirement of intent for an injunction under Section 20(b) of the 1933 Act or Section 21(e) of the 1934 Act is borne out by the provision in each section, immediately following the authorization for the SEC to seek an injunction, empowering "[t]he Commission [to] transmit such evidence as may be available concerning such acts or practices to the Attorney General who may, in his discretion, institute the necessary criminal proceedings. . . ." 15 U.S.C. §§77t(b) and 78u(e) (1970). In short, Congress itself has made separate provision for the SEC to institute civil injunction proceedings on the one hand, and to submit criminal reference reports to the Attorney General on the other hand; a showing of intent clearly is required for the latter, and equally clearly not required for the former.

(3) *Injunction to Protect Public Interest*

Third, the district court totally failed to recognize that an injunction in an SEC enforcement proceeding is sought to protect public rather than private interests. Doubts as to whether an injunction sought in such a proceeding is necessary to safeguard the public interest should be resolved in favor of granting the injunction. See *United States* v. *First National City Bank*, 379 U.S. 378, 383 (1965); *Mitchell* v. *Pidcock*, 299 F.2d 281, 287 (5 Cir. 1962). As Judge Smith recently observed, there is a vital distinction between the function of a district court in determining whether to issue an injunction in an action between

two private litigants and its function in an action by a government agency seeking an injunction to enforce an Act of Congress:

> "But the function of a court in deciding whether to issue an injunction authorized by a statute of the United States to enforce and implement Congressional policy is a different one from that of the court when weighing claims of two private litigants. . . .
>
> The passage of the statute is, in a sense, an implied finding that violations will harm the public and ought, if necessary, be restrained . . . ." *United States* v. *Diapulse Corporation of America*, 457 F.2d 25, 27-28 (2 Cir. 1972).

Not only did the district court fail to recognize this vital distinction between an injunction sought in an SEC enforcement action to protect the public interest and one sought to protect private interests in private litigation, but my colleagues appear also to have misapprehended the distinction.[39]

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39 For example, Judge Mansfield concludes his dissenting opinion thus (p. 5020, *infra*):

> ". . . I am convinced that a julgment which (1) awards compensatory damages to CCI, (2) bars BPC from voting its illegally acquired Piper shares, and (3) awards rescission to former Piper stockholders who exchanged their shares in response to BPC's tender offer, amply protects the public interest and insures against any reasonable likelihood that BPC will engage in similar conduct in the future."

Such a notion that, once private interests in separate but related litigation have been resolved, the public interest is ipso facto protected, and the need for an injunction in a separate SEC enforcement action is ipso facto eliminated, is a concept I find difficult to grasp. Surely it is a far cry from Judge Smith's perceptive recognition of "the function of a court in deciding whether to issue an injunction authorized by a statute of the United States to enforce and implement Congressional policy".

(4) *BPC's Past Violations*

Fourth, the primary factor in deciding whether past violations, now terminated, constitute a proper basis upon which to find a reasonable likelihood that defendants will commit further violations is the nature of the past violations. *SEC* v. *Manor Nursing Centers, Inc., supra,* 458 F.2d at 1100-01; *SEC* v. *Culpepper, supra,* 270 F.2d at 250; *United States* v. *W. T. Grant Co., supra,* 345 U.S. at 633.

To me, nothing could be clearer than the fact that BPC's omissions from its registration statement and prospectus—again, not minor omissions, but including a $13 million one—constituted violations of the securities laws of the most flagrant character. It was inevitable that a large loss would occur and that such loss would have an enormous impact on a company of BPC's size and character. See *SEC* v. *Texas Gulf Sulphur Co.,* 401 F.2d 833, 849 (2 Cir. 1968) (en banc), *cert. denied sub nom. Kline* v. *SEC,* 394 U.S. 976 (1969).

The district court found that such omissions were materially misleading. It nevertheless concluded that BPC did not *intentionally* or *purposefully* mislead and did not act in *bad faith.* It therefore denied the injunction. In my view, this was clearly erroneous.

On the basis of the district court's own findings, it follows as the day the night that BPC's actions were sufficiently culpable to portend that similar violations would occur in the future. A duty is imposed by law upon persons issuing securities to make a careful judgment as to what information a reasonable investor requires. BPC's management was aware of the circumstances indicating that the book value of the BAR was unrealistic. Cf. *SEC* v. *Great American Industries, Inc.,* 407 F.2d 453, 456-60 (2 Cir. 1968) (en banc), *cert. denied,* 395 U.S. 420 (1969); *Heit* v. *Weitzen,* 402 F.2d 909 (2 Cir. 1968), *cert. denied,*

395 U.S. 903 (1969). Nondisclosure of facts of a similar nature long has been condemned under the federal securities laws. BPC may not be heard to claim that its conduct in question had not been clearly declared unlawful prior to the instant suit. Cf. *SEC* v. *Keller Corp.*, 323 F.2d 397 (7 Cir. 1963).

Furthermore, BPC's misleading omissions from its registration statement and prospectus were made in the teeth of a consent decree which had been entered in the District Court for the District of Columbia on May 26, 1969 enjoining BPC from publicizing its exchange offer prior to filing a registration statement in compliance with "the registration provisions of the Federal securities laws." We recently have held that "[i]t was entirely proper to issue an injunction" when, inter alia, "appellants continued to violate the federal securities laws even after a consent decree had been entered enjoining them from such conduct." *SEC* v. *Koenig*, 469 F.2d 198, 202 (2 Cir. 1972).

Also here, as in *Koenig*, BPC and its named officers "have persisted in their contention that their past conduct was not improper". 469 F.2d at 202. This is another factor which was not taken into account, but should have been, by the district court in assessing the need for a permanent injunction. *SEC* v. *Manor Nursing Centers, Inc., supra*, 458 F.2d at 1101; *SEC* v. *MacElvain*, 417 F.2d 1134, 1137 (5 Cir. 1969), *cert. denied*, 397 U.S. 972 (1970); *Hecht Co.* v. *Bowles*, 321 U.S. 321, 331 (1944).

(5) *BPC as a Conglomerate*

Fifth, where violations of the securities laws have been committed in the past by a corporation through its officers, the nature of the corporation and its officers is an important consideration in determining the likelihood of further violations. See *SEC* v. *Texas Gulf Sulphur Co., supra,*

446 F.2d at 1306; *SEC* v. *Mono-Kearsarge Consol. Mining Co.*, 167 F.Supp. 248, 261 (D. Utah 1958). BPC is a conglomerate with holdings in diversified fields. It long has been interested in new acquisitions. Tender offers of the type involved in this litigation are becoming a popular means of achieving acquisitions. There is a reasonable likelihood that BPC will become involved in similar tender offers in the future. Such involvement is likely also to entail more battles for control.[40] As we observed in *Electronic Specialty Co.* v. *International Controls Corp.*, 409 F.2d 937, 948 (2 Cir. 1969), contests for control often are heated engagements in which both sides will resort to any means to achieve victory. It is when the temptation to violate the law is strongest that the greatest deterrence is necessary.

(6) *Abuse of Discretion*

Sixth, Judge Gurfein's opinion emphasizes that the standard for reviewing the district court's denial of injunctive relief is whether there was an abuse of discretion. I agree.

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40 Judge Gurfein's observation, "Nor do we believe that a conglomerate should be more harshly judged than others" (p. 4996 *infra*), strikes me as missing the point. I do not suggest that BPC be judged by any different *standard* than others. What I do say, as the cases hold, is that the *nature of a corporation* which has committed flagrant violations of the securities laws in the past has an important bearing upon the likelihood of recurrence of such violations. Any judge who has been required to study in depth the operations, and particularly the acquisitions, of a major conglomerate, knows that tender offers are an integral part of their way of life. See *United States* v. *International Telephone & Tel. Corp.*, 306 F.Supp. 766 (D. Conn. 1969), and 324 F.Supp. 19 (D.Conn. 1970). And any realistic estimate of the conduct of participants such as BPC and its officers in a tender offer contest, *based on their past performance in such a contest*, will acknowledge that "[t]hey act quickly, sometimes impulsively, often in angry response to what they consider, whether rightly or wrongly, to be low blows by the other side." *Electronic Specialty Co.* v. *International Controls Corp.*, *supra*, 409 F.2d at 948.

I stand four square on what I said in *SEC* v. *Manor Nursing Centers, Inc., supra*:

> "In an action, such as the instant one, where the SEC sought injunctive relief under Section 20(b) of the 1933 Act, 15 U.S.C. §77t(b) (1970), and under Section 21(e) of the 1934 Act, 15 U.S.C. §78u(e) (1970), a district court has broad discretion to enjoin possible future violations of law where past violations have been shown, and the court's determination that the public interest requires the imposition of a permanent restraint should not be disturbed on appeal unless there has been a clear abuse of discretion. SEC v. Texas Gulf Sulphur Co., 446 F.2d 1301, 1306-7 (2 Cir.), cert. denied, 404 U.S. 1005 (1971); SEC v. Culpepper, 270 F.2d 241, 250 (2 Cir. 1959). *Moreover, the party seeking to overturn the district court's exercise of discretion has the burden of showing that the court abused that discretion, and the burden necessarily is a heavy one.* SEC v. Culpepper, *supra*, 270 F.2d at 250; United States v. W. T. Grant Co., 345 U.S. 629, 633 (1953). In the instant case, we hold that appellants have not sustained that burden, for the record amply supports the district court's conclusion that the issuance of a permanent injunction was appropriate." (emphasis added) 458 F.2d at 1100.

Of course, our appellate review in *Manor Nursing* was addressed to the *grant* of an injunction in an SEC enforcement proceeding. Here we are reviewing the *denial* of such an injunction. Our scope of review would appear to be different. As Judge Waterman stated in *NMU* v. *Commerce Tankers Corp.*, 457 F.2d 1127 (2 Cir. 1972):[41]

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41 *Commerce Tankers* involved the denial of an injunction authorized pursuant to an Act of Congress, i.e. Section 10(*l*) of the National Labor Relations Act, 29 U.S.C. §160(*l*) (1970).

> "Were this an appeal from the *grant* after an evidentiary hearing of [an] injunction our scope of inquiry could be limited by the 'clearly erroneous' test. However, when the appeal is from the *denial* of a petition for [an] injunction, it seems that, in light of the congressional policy favoring the grant of such injunctions in appropriate circumstances, our scope of review ought not to be so limited." (emphasis that of the Court) 457 F.2d at 1133-34.

In any event, whatever abuse of discretion standard be applied, in my view the district court's denial of an injunction here was a plain abuse of discretion—even on the record then before the court.[42] And surely, in view of our decision today holding that BPC's conduct constituted flagrant violations of the antifraud provisions of the federal securities laws—a holding of course unknown to the district court when it denied the permanent injunction—it would seem to me that at the very least we should remand the case to the district court, as we did in *SEC* v. *Texas Gulf Sulphur Co., supra,* "for a further determination below, in the light of the approach explicated by us in [our opinion filed today] as to whether, in the exer-

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42 Judge Grufein refers to "the experienced trial Judge below . . . a trial judge experienced in the securities field." I agree that Judge Pollack is indeed a trial judge thoroughly experienced in this field. And I yield to no judge on our Court in my firm belief that a district judge's exercise of discretion should not be reversed absent a clear showing of abuse; the record of decided cases in our Court bears this out.

But it does strike me that all of this begs the question. After more than a dozen years on the federal bench—mostly as a district judge—I have never discerned any notable reticence on the part of federal appellate judges about reversing a district judge upon a showing of abuse of discretion. Indeed, the benchmark of a truly competent district judge—as with Judge Pollack in the instant case—is his capacity to insure that the record demonstrates with crystal clarity the basis of his exercise of discretion, so that a reviewing court can determine abuse or the absence of abuse.

cise of its discretion, the injunction against [BPC] which the Commission seeks should be ordered." 401 F.2d at 864.

(7) *Mischievous Precedent*

Finally, today's judgment and opinion by the majority of this panel affirming the denial of a permanent injunction in this SEC enforcement action, in my opinion, will cause mischief in the enforcement of the federal securities laws.

The decision undercuts the strong policy of this Court of encouraging vigorous enforcement of the securities laws. Its radiations will have their impact beyond this Circuit, since other courts look to us for guidance in this area.

In my view, no decision during the four decades the federal securities laws have been on the books will more effectively cripple the salutory enforcement program of the Securities and Exchange Commission than today's 2-1 decision by the majority of this panel on this issue.

I therefore respectfully but most emphatically dissent from the denial of a permanent injunction.

I would hold that the district court erred in denying the SEC's request for a permanent injunction against further violations of the securities laws; and I would remand with directions that the district court issue such an injunction.

(B) Rescission Order

The district court concluded that BPC would be required to make an offer of rescission to former Piper shareholders who accepted the BPC exchange offer. It directed the parties to submit an appropriate decree for the court's consideration. 331 F.Supp. at 1162.

The decree as entered provided, among other conditions not contested on appeal, that if the rescinding Piper share-

holder previously had sold the BPC securities received in the exchange offer, he must tender to BPC—in addition to the amount of securities he received plus dividends and interest paid (or due and payable) thereon—a cash payment equal to the excess, if any, of his sales proceeds from the original BPC securities over his cost of repurchasing the substitute BPC securities which he tenders to BPC. Both parties on appeal challenge the rescission order but for different reasons.

Before considering the propriety of the district court's order, we must decide whether a federal district court has the power, at the request of the SEC, to order rescission or restitution. The SEC has no express statutory authority to seek rescission, restitution, or other forms of equitable monetary relief. The Commission, however, may institute an action for injunctive relief and, once the equity jurisdiction of the district court has been properly invoked, the court has power to grant all equitable relief necessary under the circumstances. *SEC* v. *Manor Nursing Centers, supra*, 458 F.2d at 1103-04, and authorities there cited. See generally 1 Pomeroy, Equity Jurisprudence §236a (5th ed. 1941). As the Supreme Court said in an analogous situation:

> "When Congress entrusts to an equity court the enforcement of prohibitions contained in a regulatory enactment, it must be taken to have acted cognizant of the historic power of equity to provide complete relief *in light of the statutory purpose.*" *Mitchell* v. *Robert DeMario Jewelry, Inc.*, 361 U.S. 288, 291-92 (1960). (Emphasis added).

Accord, *SEC* v. *Texas Gulf Sulphur Co., supra*, 446 F.2d at 1307-08. Ancillary relief contributes to effective enforcement of the securities laws by depriving defendants of gains made through violations, by deterring future vio-

lations, and by increasing the overall efficiency of Rule 10b-5 and similar actions. See generally Note, *Ancillary Relief in SEC Injunction Suits for Violation of Rule 10b-5*, 79 Harv. L. Rev. 656 (1966). Accordingly, we hold that the SEC can seek ancillary equitable relief where, as in the instant action, it is necessary to effectuate the statutory purpose.

BPC challenges the rescission order on the ground that a former Piper shareholder who has disposed of the BPC securities he received on the exchange offer should not be eligible for rescission. It argues that, since a Piper shareholder so situated could not obtain rescission if he brought the action himself, the SEC should not be permitted to seek rescission for him. The defect in this argument is that a Piper shareholder could purchase substitute shares and demand rescission if he brought his own rescission action. BPC maintains that a shareholder can sue only under §11 or §12(2) of the 1933 Act and that neither of those provisions permits rescission where the plaintiff no longer holds the shares. We need not decide whether BPC's interpretation of these provisions is correct because a defrauded shareholder also can bring suit for rescission and restitution under §10b of the 1934 Act, *Errion* v. *Connell*, 236 F.2d 447 (9 Cir. 1956), or under §29(b) of the 1934 Act, *Geismar* v. *Bond & Goodwin, Inc.*, 40 F.Supp. 876 (S.D.N.Y. 1941). Although the issue appears not to have been resolved, it is reasonable to assume with respect to such claims that a shareholder seeking rescission, even if he has disposed of his shares, should be permitted to tender substitute shares. See Restatement of Restitution §66(4) (1937); 3 Loss, Securities Regulation 1792-93 (2d ed. 1961, Supp. 1969). Furthermore, the SEC requests this rescission order not merely to compensate Piper shareholders for their loss but also to implement the broader statutory purpose of protecting the public

interest through effective enforcement of the securities laws. Limitations on the relief available in actions brought by private parties are not necessarily applicable to SEC enforcement proceedings. We hold that the district court was correct in permitting former Piper shareholders who had disposed of the BPC securities received on the exchange offer to tender substitute shares.

The SEC challenges the condition of the rescission order that requires a tendering Piper shareholder to return any profit he may have realized from the sale of his BPC securities and the purchase of substitute shares on the present market at a lower price. It is true that a prerequisite to the remedy of restitution is that a party seeking rescission must return any proceeds he has received from the transaction being rescinded in order to be placed in *status quo ante*. *Mott* v. *Tri-Continental Financial Corp.*, 330 F.2d 468, 470-71 (2 Cir. 1964). But the "proceeds" that must be returned are those received as consideration from the other party. That does not necessarily include profits realized from an interim sale resulting from fortuitous events which occurred subsequent to the transaction. It would be inequitable to require the tender of these profits where, as here, the other party is not required concomitantly to underwrite losses. The effect of the condition imposed by the district court is to render ineffective the rescission remedy.[43]

We hold that the district court erred in imposing the condition requiring restitution of interim profits; and we remand with directions that the judgment be modified by deleting that condition from the rescission order.

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43 There can be no expectation that the Piper shareholders will tender unless the market for their shares upon rescission is an open and free one. Such a market cannot exist where the price to be paid for the assignment of a right by each individual Piper shareholder is subject to different fact situations.

On its cross-appeal, BPC argues with regard to its exchange offer that it did not fail to disclose facts which a reasonably prudent investor would deem to be material. We have dealt with this issue at length in our opinion above in *Chris-Craft Industries, Inc.* v. *Piper Aircraft Corporation, et al.* (No. 72-1064). Our decision on this issue there is conclusive here.

On the SEC's appeal in No. 72-1053, to the extent the judgment is appealed from, we affirm in part, and reverse and remand in part. On BPC's cross-appeal in No. 72-1140, we affirm.

SUMMARY

The following is a summary of our essential holdings in each of the three appeals.

In CHRIS-CRAFT INDUSTRIES, INC. v. PIPER AIRCRAFT CORPORATION, ET AL. (No. 72-1064). we hold that:

(1) Chris-Craft has standing under the antifraud provisions of §14(e) of the 1934 Act to sue defendants for damages.

(2) The record establishes violations of §14(e) on the part of all defendants, i.e. the Piper family defendants (not the Piper Aircraft Corporation); Bangor Punta Corporation and its named officers; and the First Boston Corporation and its named officers.

(3) Under appropriate principles of causation, the acts and conduct of each of the defendants in violation of §14(e) caused injury to Chris-Craft for which it is entitled to be compensated.

(4) Chris-Craft also is entitled to recover damages from Bangor Punta for the injury caused by Bangor Punta's cash purchases of large blocks of Piper

stock during the pendency of Bangor Punta's exchange offer for Piper shares, in violation of Rule 10b-6 under the 1934 Act.

(5) The judgment of the district court dismissing the complaint is reversed and the case is remanded with directions to enter judgment awarding damages and equitable relief in accordance with our opinion.

In BANGOR PUNTA CORPORATION v. CHRIS-CRAFT INDUSTRIES, INC. (No. 72-1120), we hold that:

(1) Bangor Punta failed to prove its claim of unlawful market manipulation of Chris-Craft stock.

(2) Bangor Punta failed to prove its claim of illegal warehousing of Chris-Craft stock.

(3) The judgment of the district court dismissing the complaint is affirmed on the ground that Bangor Punta failed to adduce sufficient evidence to support its claims that Chris-Craft violated the securities laws or that such violations caused injury to Bangor Punta.

In SEC v. BANGOR PUNTA CORPORATION (Nos. 72-1053 and 72-1140), to the extent the judgment is appealed from, we hold that:

(1) The district court did not err in denying the SEC's request for a permanent injunction against further violations by Bangor Punta of the securities laws.

(2) The district court erred in imposing, as a condition to its order that Bangor Punta offer rescission to all Piper shareholders who had accepted Bangor Punta's exchange offer, the requirement that such shareholders make restitution of any interim profits realized by them on the sale of their Bangor Punta

securities; and the case is remanded with directions that the judgment be modified by deleting that condition from the rescission order.

(3) On Bangor Punta's cross-appeal, we affirm the judgment of the district court.

CHRIS-CRAFT v. BANGOR PUNTA

GURFEIN, *District Judge*, concurring.

I concur generally in Judge Timbers' scholarly opinion except as to the injunction sought by the SEC.

In view of the apparent disparity between the views of my brothers I respectfully comment on some of the points raised.

STANDING

With respect to standing I am inclined to agree with Judge Mansfield that there is no constitutional question. My approach is, moreover, much closer to Judge Pollack's though I disagree with his conclusion. It seems to me he was right in approaching the problem as one of causation before considering the question of standing. If there is no causation standing becomes a rather abstract conception. Since the seven per cent illegally acquired by BPC caused it to win the contest, the loser has standing. I think it unnecessary to say that a defeated contender who won a booby prize of say, one per cent of the stock, would have standing simply because he entered the lists and lost.

SCIENTER AND CAUSATION

I agree that some kind of scienter must be shown. But I do not think a litmus paper test of scienter will ever

be found. I am content to accept the general formulation that mere negligence will not suffice in a private action for money damages and that "recklessness that is equivalent to wilful fraud," *SEC* v. *Texas Gulf Sulphur Co.*, 401 F.2d 833, 868 (Friendly, *C.J.* concurring), is required for a violation of Section 14(e) as well as of Section 10(b). In modern times statutory construction grows case by case much as the common law did when more general rules of law were involved. And I venture to say that stability may be more easily attained by analogizing from decided cases whose facts are known than by guessing what may come within some general rule which must of necessity be inchoate if only for want of the gift of prophecy.

§10(b)(6)

With respect to the Section 10(b)(6) violation I limit my concurrence to agreement that there was such a violation as we held in *Chris-Craft Industries, Inc.* v. *Bangor Punta Corp.*, 426 F.2d 569, 576-77 (2 Cir. 1970), and would hold that since the block purchases were necessary for control causation was established. I do not think we are required in this case to pass more precisely on the general question whether a purchase off the market that does not affect the tape causes price fluctuations and damage simply because it is a violation of Section 10(b)(6). On that question Judge Pollack, in my respectful submission, was right.

SECURITIES AND EXCHANGE COMMISSION, PLAINTIFF-APPELLANT-APPELLEE v. BANGOR PUNTA CORPORATION, DEFENDANT-APPELLEE-APPELLANT

INJUNCTIVE RELIEF

Judge Mansfield and I do not agree that Judge Pollack's denial of injunctive relief to the SEC against BPC should

be reversed. We respectfully suggest that the matter is not so clear that we should substitute our judgment for the judgment of the experienced trial Judge below who sat as a chancellor in equity. He heard the witnesses and had the opportunity by observation better to prophesy future conduct than we can on this printed record.

The days are long since past when appellate courts in the federal system in equity cases reviewed findings of fact *de novo*. The scope of appellate review is more sharply limited even in causes that would have been formerly classed as proceedings in equity. The findings of the trial Court must be clearly erroneous or they will not be set aside. Fed.R.Civ.P. 52(a).

Specifically, the test for review of the denial of injunctive relief is whether there has been an abuse of discretion. See *United States* v. *W.T. Grant Co.*, 345 U.S. 629, 633, 634 (1953). In *United States* v. *W.T. Grant Co.* the Supreme Court said that for reversal "the Government must demonstrate that there was no reasonable basis for the District Judge's decision." 345 U.S. at 634. And this Court has recognized that this rigorous limitation on appellate review applies to SEC actions for injunctive relief as well. As was said in *SEC* v. *Manor Nursing Centers Inc.*, 458 F.2d 1082, 1100 (2 Cir. 1972), "the party seeking to overturn the district court's exercise of discretion has the burden of 'showing that the court abused that discretion, and the burden necessarily is a heavy one.' *SEC* v. *Culpepper, supra*, 270 F.2d at 250; *United States* v. *W.T. Grant*, 345 U.S. 629, 633 (1953)." I think we lose sight of these accepted principles if we reverse and order the issuance of a permanent injunction in this case.

Here Judge Pollack found against the SEC on its primary contention. He found that there was no purposeful withholding of the completion of the Dumaine negotiation

until the contest for Piper was over. 331 F.Supp. 1154 at 1160. We cannot set this finding aside as clearly erroneous on this record. This is a weighty finding by a trial Judge experienced in the securities field. In the last analysis we are dealing with intent and must seek to determine whether there is a likelihood of recurrence of unlawful activity and a need for a prophylactic against recidivism. Who is better able to determine such things than the Judge who saw and heard the witnesses and got the feel of what happened?

In the opinion in the other cases decided today, we accept the District Court's "inferences drawn from undisputed evidence" that the delay in consummating the deal resulted from a prudent business decision to investigate the legal and accounting impact of the sale.

Judge Timbers argues that there is a "core" difference between the standard of "a propensity or natural inclination to violate the securities law" attributed to Judge Pollack, and the test offered by Judge Timbers' opinion "whether there is a reasonable likelihood that the wrong will be repeated." Of course the statute expresses it as "any person [who] is engaged or about to engage in any acts or practices which constitute or will constitute a violation." The use of either test, if indeed they differ except in verbiage, is not the subject of immutable statutory command. We do not see sufficient difference in the standards juxtaposed to find that the District Court erred as a matter of law. Indeed, if one wished to be finicky, Judge Timbers' formulation is the more limited—"*the* wrong will be repeated" implying a rather narrowly repetitive violation while the propensity standard covers a multitude of violations (emphasis supplied). We emphasize that we are not in the least interested in limiting the basis for an SEC injunction as a matter of general rule.

The dissent also misinterprets our view on intent. We are not limiting our injunctive relief to common law fraud as is implied from the citation of *SEC* v. *Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 200 (1968). Nor are we eliminating reckless conduct that may be tantamount to culpable negligence from the proper basis for injunctive relief at the instance of the Commission. Nor do we treat as unimportant the public interest as is suggested.

Since we do not deny that in a proper case even sustained recklessness can be the basis for injunctive relief there is no such divergence of opinion in the abstract as Judge Timbers suggests. We repeat that we are not the finders of fact. The impact of our decision is, by its terms, limited to the scope of appellate review.

In *Texas Gulf Sulphur, supra,* this Court simply remanded "the cause as to it [Texas Gulf Sulphur Company] for a further determination *below,* in the light of the approach explicated by us in the foregoing opinion, as to whether in the exercise of *its* discretion, the injunction against it which the Commission seeks should be ordered" (emphasis supplied). And as Chief Judge Friendly said in concurring: "Absent much clearer language than is found in the 1934 Act, the entitlement of a plaintiff to an injunction thereunder remains subject to principles of equitable discretion." He pointed out that Judge Bonsal had acted on the erroneous belief that "no violation of the Rule had occurred and he was without power to enjoin," but Chief Judge Friendly wrote: "If Judge Bonsal had denied an injunction on these grounds [i.e. 'no danger of repetition'], I see no basis on which we could properly have reversed him." 401 F.2d at 869.

In the instant case the District Judge found that the omission in the registration statement was material, but in his discretion, considering the public interest, he did not

enjoin because he did not believe there was likelihood of recurrence. 331 F.Supp. at 1162-63. We do not consider that to be such an abuse of discretion as to support reversal. And "abuse of discretion" it would have to be. See *Hecht Co.* v. *Bowles*, 321 U.S. 321, 331 (1944).

Nor do we believe that a conglomerate should be more harshly judged than others. The issue is not whether it will seek other acquisitions but rather how it will go about doing them.

In any event sanctions need not be cumulative. Damages tend to have a didactic effect. The SEC has, through our decision in the companion cases now largely achieved its commendable purpose. Further to enjoin we think would be to add yet another star to the flag of a battle already won. The denial of an injunction is affirmed.

MANSFIELD, *Circuit Judge* (Concurring and Dissenting):

I concur in those results reached in Judge Timbers' opinion which represent the majority opinion as to issues other than injunctive relief, except that I dissent from the reversal of the district court's dismissal of CCI's suit against the Piper family defendants.

I also concur in Judge Gurfein's opinion to the extent that it represents the majority decision affirming the denial of injunctive relief.

With due respect for my brother Timbers' exhaustive analysis of these complicated cases in his opinion ("main opinion" herein), I find myself in disagreement with some of his conclusions and reasoning. I would also limit our discussion to those legal principles necessary for adjudication of the issues presented rather than engage in unnecessary dicta in this sensitive area. The Supreme Court has urged that judicial construction of the anti-fraud provi-

sions of the federal securities laws be limited to what is essential for the decision at hand:

> "Although §10(b) and Rule 10b-5 may well be the most litigated provisions in the federal securities laws, this is the first time this Court has found it necessary to interpret them. We enter this virgin territory cautiously. The questions presented are narrow ones. They arise in an area where glib generalizations and unthinking abstractions are major occupational hazards. Accordingly, in deciding this particular case, remembering what is not involved is as important as determining what is. With this in mind, we turn to respondents' particular contentions." *SEC* v. *National Securities, Inc.*, 393 U.S. 453, 465 (1969).

Several points discussed in Judge Timbers' opinion, while interesting, strike me as both irrelevant to the issues and as a source of possible confusion to readers. Other observations go much further than is necessary. With still others I must respectfully disagree. For these reasons I find it necessary to state my own differing views in this area. In doing so I shall follow the sequence of the main opinion.

Function of Private Damage Suits

I agree that the anti-fraud and anti-manipulation sections of the federal securities laws were designed to insure against distortion and falsity in the purchase and sale of securities, and that private damage suits based upon violation of those laws should be encouraged as a means of supplementing governmental action in the vigorous enforcement of those laws. See *J. I. Case Co.* v. *Borak*, 377 U.S. 426 (1964); Fleischer, *"Federal Corporation Law": An Assessment*, 78 Harv. L. Rev. 1146, 1172-79

(1965); Lowenfels, *Implied Liabilities Based Upon Stock Exchange Rules,* 66 Colum. L. Rev. 12; Lowenfels, *Private Enforcement in the Over-the-Counter Securities Markets; Implied Liabilities Based on NASD Rules,* 51 Cornell L.Q. 633 (1966). However, it is unrealistic and fanciful to suggest that through such suits "society can obtain the maximum amount of its preferred goods and services that our resources can produce."

Full disclosure may go far toward achieving a fair and honest marketplace for trading of securities. But honesty cannot be equated with efficiency in the use of funds or assets realized from a public issue or tender offer. One need only look at the dockets of our federal district courts to appreciate that bankruptcies of honest entrepreneurs are all too common.

CCI's Standing

With due respect for the views of the author of the main opinion, the issue before us is not whether "CCI has standing in a constitutional sense." If that were the issue, it could be settled by a one-line reference to the Supreme Court's decision in *Association of Data Processing Service Organizations, Inc.* v. *Camp,* 397 U.S. 150 (1970). The issue is one of statutory construction: Does §14(e) confer standing upon a defeated competitor for control to sue the successful party for damages based on its violation of the anti-fraud provisions of the securities acts?

The federal securities laws are silent on the subject of a private party's standing to sue. Indeed, neither §14(e) nor §10(b) or Rule 10b-5 state that purchasers, sellers, or exchangers of securities have the right to sue. However, their implied standing to sue has long since been judicially established, *Kardon* v. *National Gypsum Co.,* 69 F. Supp. 512 (E.D. Pa. 1946). I would recognize CCI's standing solely on the ground that vigorous enforcement of the

anti-fraud provisions through private litigation, *J. I. Case Co.* v. *Borak*, 377 U.S. 426 (1964), calls for similar implication of a private right of action in favor of a defeated contestant against the successful bidder for control for damages caused by the latter's violation of that section, see *Crane Co.* v. *Westinghouse Air Brake Co.*, 419 F.2d 787 (2d Cir. 1969), *cert. denied*, 400 U.S. 822 (1970), especially in view of our willingness to permit the target corporation to seek relief against the offeror under §14(e). *Electronic Specialty Co.* v. *International Controls Corp.*, 409 F.2d 937 (2d Cir. 1969); *Butler Aviation International Inc.* v. *Comprehensive Designers, Inc.*, 425 F.2d 842 (2d Cir. 1970).

Scienter

It is generally agreed in this Circuit that some form of *scienter* is required to support a private damage claim based upon a violation of Rule 10b-5, compare *SEC* v. *Texas Gulf Sulphur Co.*, 401 F.2d 833, 855, 863, 866-68 (Friendly, Ch. J., concurring) (2d Cir. 1968) (*en banc*), *cert. denied sub nom. Kline* v. *SEC*, 394 U.S. 976 (1969), with *Globus* v. *Law Research Service, Inc.*, 418 F.2d 1276, 1290 (2d Cir. 1969), *cert. denied*, 397 U.S. 913 (1970), and while less than the specific fraudulent intent required to prove common law fraud will suffice, mere negligence is not enough, *Shemtob* v. *Shearson, Hammill & Co.*, 448 F.2d 442, 445 (2d Cir. 1971).[1] No reason has been advanced for a different standard in the enforcement of §14(e), the language of which is substantially the same as that found in §10(b) and Rule 10b-5.

In the present case, although an intent to defraud has not been shown, defendants' conduct amounted to more than mere negligence. Our answer to the question of

1 See VI L. Loss, Securities Regulation 3883-88 (Supp. to 2d ed. 1969).

whether the proof was sufficient to satisfy the *scienter* requirement depends, therefore, upon the standard that is to govern the gray area between the extremes of specific fraudulent intent, on the one hand, and mere negligence, on the other. In my view that standard cannot be satisfactorily described in such abstract terms as "culpability," a generality frequently associated with any blameworthy or even criminal conduct, see I Working Papers of the National Committee on Reform of Federal Criminal Laws 123 (July 1970), much less as "fraud," "constructive fraud," "bad faith" or various gradations of "recklessness."

If there is to be a meaningful *scienter* standard, it should, if possible, be stated in more specific terms. Of course it might vary according to the existence of a fiduciary relationship, the burden of proof and the nature of the relief sought.[2] It might also take into account the nature and duties of the corporate posts held by the defendants, whether they are insiders or outsiders, and whether they are active or inactive participants. See generally Mann, *Rule 10b-5: Evolution of a Continuum of Conduct to Replace the Catch Phrases of Negligence and Scienter*, 45 N.Y.U.L. Rev. 1206 (1970). However, if we are unable to state a standard with some degree of precision, we should frankly confess that the only method of describing the element of *scienter* is by illustration rather than by categorization or rule of general application. See, e.g., Bucklo, *Scienter and Rule 10b-5*, 67 Nw. U.L. Rev. 562, 568 (1972). *Scienter*, like obscenity, would then simply be

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2 We have indicated that the *scienter* requirement in suits for injunctive relief may be less strict than that in damage actions. *Mutual Shares Corporation* v. *Genesco Inc.*, 384 F.2d 540, 547 (2d Cir. 1967); *SEC* v. *Texas Gulf Sulphur Co.*, 401 F.2d 833, 863 (per Waterman, J.), 866-68 (Friendly, J., concurring) (2d Cir. 1968), *cert. denied sub nom. Kline* v. *SEC*, 394 U.S. 976 (1969); *SEC* v. *Great American Industries Inc.*, 407 F.2d 453, 463 (2d Cir. 1968) *(en banc), cert. denied*, 395 U.S. 920 (1969) (concurring opinion of Kaufman, J.).

something recognized when seen, but not otherwise definable. Cf. *Jacobellis* v. *Ohio*, 308 U.S. 184, 197 (1964) (Stewart, J., concurring) ("I shall not attempt further to define the kinds of material. . . . But I know it when I see it. . . ."). But I believe that an applicable *scienter* rule can be formulated and defined.

Congress' use of the words "fraudulent," "deceptive" and "manipulative" in §14(e), when coupled with the partially similar language and the legislative history of the earlier-enacted §10(b), indicates that its purpose was not to punish mere negligence, see S. Rep. 792, 73d Cong., 2d Sess. 6 (1934), *Kohn* v. *American Metal Climax Inc.*, 458 F.2d 255, 279-80 (3d Cir. 1972) (concurring and dissenting opinion of Adams, J.), but that the law was aimed at misrepresentations or omissions involving *some degree of awareness* on the part of the corporate officer charged. If Congress had intended to impose absolute liability, subject to a "due diligence" or "good faith" defense, it could have used language similar to that found in §11 of the 1933 Act. If, on the other hand, it had intended to limit liability to willful and intentional misrepresentation, it could have used language similar to that found in §9(e) of the 1934 Act, 15 U.S.C. §78i(e) (making liable any person who "willfully participates" in the sale of securities, *inter alia*, through use of materially false or misleading statements, §9(a)(4)). The words "manipulative," "deceptive," and "fraudulent," as applied to statements or omissions, seem to have been intended to have a meaning similar to that later ascribed to them by the Commission, which has defined misleading statements or omissions as those "made with knowledge or reasonable grounds to believe that [they are] untrue or misleading," 17 C.F.R. §240.15c 1-2(b).

When §§10b and 14(e) are viewed against the entire background and purpose of the securities laws, the *scienter*

requirement would be satisfied upon a showing that the person charged knew the material facts misstated or omitted and could reasonably have been expected to appreciate their significance, see *Heit* v. *Weitzen*, 402 F.2d 909, 914 (2d Cir. 1968), or, if he did not know them, that he had reasonable cause to believe that there might be a material failure in disclosure and yet did not ascertain and disclose the facts even though he could have done so without any undue effort. In short, the *scienter* requirement would be met if the corporate officer (1) knew the essential facts and failed to disclose them, or (2) failed or refused, after being put on notice of a possible material failure in disclosure, to apprise himself of the facts under circumstances where he could reasonably have ascertained and disclosed them without any extraordinary effort.

In keeping with the broad remedial aims of the anti-fraud provisions of the federal securities laws such a standard of responsibility, while requiring proof of more than mere negligence, would not permit top corporate officers and those aiding and abetting them to escape liability by pleading ignorance where it can be shown that red flags putting them on notice or providing warning signals of either undisclosed or misrepresented facts of a material nature were readily apparent to all and that a routine check would have disclosed the misrepresentation. Such a test would also serve to differentiate §§14(e), 10(b) and Rule 10b-5 and §17(a) of the 1933 Act, 15 U.S.C. §77q, see *SEC* v. *Texas Gulf Sulphur, supra* at 867 (Friendly, Ch. J., concurring), on the one hand, from other provisions of the securities acts, such as §§11, 12(1), 12(2), 15 U.S.C. §§77k, 77l(1), (2), which impose upon persons charged the burden of proving "due diligence," see *Escott* v. *Barchris Construction Corp.*, 283 F. Supp. 643, 682-703 (S.D.N.Y. 1968).

Since the defendants in the present case had knowledge of the material facts misstated or omitted or had sufficient

notice of possible misstatements and could reasonably have ascertained the facts with a minimum of effort, the proof clearly satisfies the standard.

The majority opinion gives lip service to the foregoing test but adds a series of qualifications and characterizations that in my view are unnecessary and only serve to cast doubt upon the standard itself. The effect is to compound existing confusion as to the law in the area. Starting with the view that proof of *scienter* requires a showing of "culpability" the main opinion translates that term into "knowing or reckless failure" to ascertain and disclose those facts as to which the person sued has a "duty of disclosure." With respect to the nature and extent of this duty, we are provided with uncertain and apparently conflicting guidelines. Although the duty is described as one which requires the corporate officer to "act reasonably in discovering facts material to the [exchange] offer," *ante* at 38, that statement is promptly qualified by observations to the effect that "corporate officers have a reasonable area of discretion in determining how far to explore the facts and in deciding what facts need to be disclosed," *id.*, and that they must be allowed "considerable room" for such discretion, *supra*, n.22. With these latter comments I must respectfully disagree. In my view the test of materiality which was adopted by this court in *List*, *Heit* and *Texas Gulf Sulphur*, remains an objective one. If the corporate officer has knowledge of facts that are material according to that test, he cannot in his discretion decide not to disclose them without facing liability under §14(e).

Reliance

On the subject of what proof of reliance is required to establish causation, the Supreme Court has spoken definitively in *Mills* v. *Electric Auto-Lite Co.*, 396 U.S. 375 (1970), and in its sequel, *Affiliated Ute Citizens* v. *United*

States, 406 U.S. 128 (1972). In *Mills* minority shareholders of Electric Auto-Lite brought a derivative and representative class action challenging that company's merger with Mergenthaler Linotype Company on the ground that stockholders' approval had been obtained by means of a materially misleading proxy statement in violation of §14(a) of the Securities Exchange Act of 1934, 15 U.S.C. §78n(a), and SEC Rule 14a-9. The alleged omission was the failure of defendants, who controlled 54% of Auto-Lite's voting shares and needed a two-thirds majority for approval of the merger, to disclose that they were nominees of Mergenthaler. The district court's award of summary judgment to the plaintiffs was reversed by the Court of Appeals on the ground that causation had not been established. The Supreme Court, in a characteristically lucid opinion by Justice Harlan, who spoke for a unanimous court, reversed the Court of Appeals, holding that where the "proxy solicitation itself, rather than the particular defect in the solicitation materials, was an essential link in the accomplishment of the transaction," 396 U.S. at 385, proof of actual reliance on the material misstatement or omission need not be adduced. This principle was later summarized by Justice Blackmun in *Affiliated Ute Citizens, supra*, as follows:

> "Under the circumstances of this case, involving primarily a failure to disclose, positive proof of reliance is not a prerequisite to recovery. All that is necessary is that the facts withheld be material in the sense that a reasonable investor might have considered them important in the making of this decision. See *Mills* v. *Electric Auto-Lite Co.*, 396 U.S. 375, 384 (1970); *SEC* v. *Texas Gulf Sulphur Co.*, 401 F.2d 833, 849 (CA2 1968), cert. denied *sub nom. Coates* v. *SEC*, 394 U.S. 976 (1969); 6 L. Loss, Securities Regulation 3876-3880 (1969 Supp. to 2d ed. of Vol. 3); A. Brom-

berg, Securities Law, Fraud—SEC Rule 10b-5, §§2.6 and 8.6 (1967). This obligation to disclose and this withholding of a material fact establish the requisite element of causation in fact. *Chasins* v. *Smith, Barney & Co.*, 438 F.2d at 1172." 406 U.S. at 153-54.

In short, whatever may have been our earlier views as to the necessity of adducing positive proof of reliance, see, e.g., *Green* v. *Wolf Corp.*, 406 F.2d 291, 301 (2d Cir. 1968), cert. denied, 395 U.S. 977 (1969), the gravamen of the offense is now the material misrepresentation itself, from which reliance by a reasonable investor may be inferred as a matter of law, thus rendering unnecessary proof of actual subjective reliance. The rationale behind this doctrine is that it "will avoid the impracticalities of determining how many votes were affected, and, by resolving doubts in favor of those the statute is designed to protect, will effectuate the congressional policy of ensuring that the shareholders are able to make an informed choice when they are consulted on corporate transactions." 396 U.S. at 385.

The main opinion, following the lead of Judge Adams in *Kohn* v. *American Metal Climax Inc.*, 458 F.2d 255, 290 (3d Cir. 1972), construes *Mills-Ute* as creating a *"presumption"* of reasonable reliance "where it is logical to presume that reliance in fact existed." I disagree with this interpretation of the Supreme Court's decisions on the subject. At no point did that Court expressly or impliedly speak in terms of a "presumption." Use of that term naturally raises further questions: Is the presumption to be conclusive or rebuttable? If rebuttable, should not BPC be given an opportunity in the present case to rebut the presumption by offering proof that the percentage of Piper shareholders who did not rely upon its alleged

misrepresentations in tendering their shares was sufficient to enable BPC to achieve control? See Note, *Causation and Liability in Private Actions for Proxy Violations,* 80 Yale L.J. 107, 135-38 (1970).

In my view, unless reasonable reliance is found as a matter of law on the basis of the material misrepresentation, the Supreme Court's purpose in *Mills-Ute,* which was to avoid the impracticalities of determining how many votes or decisions to tender were affected, would be undermined. The door would still be open to extensive discovery and protracted proceedings aimed at establishing subjective non-reliance. The Supreme Court's decision not to remand for introduction of such proof in *Mills* or *Ute* indicates that it established a rule of law rather than a "presumption." Moreover, *Ute,* which involved 10b-5 claims, refutes the distinction relied on by Judge Adams in *Kohn, supra* at 289, that different standards of reliance and causation may be applicable to claims under §14(a) as opposed to those under §10(b).

In the present case BPC needed all but approximately 1% of the 7% gained as a result of its exchange offer in order to achieve its 51% control. Proof of non-reliance by all but 1% of the tendering Piper shareholders would be most unlikely. However, the main opinion, *ante* at 43, by obligating CCI to "show that there was a misrepresentation upon which the target corporation stockholders relied and that this was in fact the cause of CCI's injury" and by stating repeatedly that reliance will be "presumed," virtually invites an application for rehearing and remand to try the issue of reliance. I would clarify that issue now.

For these reasons my concurrence is based simply upon the view that, according to the principles established by the Supreme Court in *Mills* and *Ute,* CCI has established reliance as a matter of law in the present case.

BPC's Violations of Rule 10b-6 of the 1934 Act

In its denial of preliminary injunctive relief this court held that BPC's cash purchases of 120,200 Piper shares violated Rule 10b-6. *Chris-Craft Industries, Inc.* v. *Bangor Punta Corp.*, 426 F.2d 569, 576-77 (2d Cir. 1970) (*en banc*). We there found Rule 10b-6 applicable to purchases of a target corporation's shares since such purchases might have a bullish radiating effect upon a pending exchange offer.

I concur in the view that since BPC's unlawful purchases of Piper shares enabled it to gain control of Piper, its conduct is actionable at the instance of CCI, which was thereby handicapped in its lawful competition for control. However, I cannot agree with the main opinion's view that BPC's purchases actually "operated in the market to make BPC's exchange offer deceptively attractive." There was no such proof. Nor do I accept the view that liability should be predicated upon the *"presumption"* that "Piper shareholders . . . were deceived" or that the "illegal purchases will substantially inflate" the price of the exchange offer. Unless the presumption were conclusive, BPC would be entitled to rebut it by offering proof that its cash purchases did not have any radiating effect upon the exchange offer.

For these reasons my concurrence is based solely on the ground that where a party acquires control of a target corporation through violation of applicable provisions of the securities acts and regulations promulgated thereunder (in this case Rule 10b-6), it is liable as a matter of law to a competitor for any damages caused by the illegal conduct.

The Piper Family Defendants

I concur in the conclusion that the Piper family defendants did not become liable to CCI by virtue of their participation in the May 8th press release announcing the BPC exchange offer. The statement of predicted value contained

in the release was not a material representation since the specific terms were contained in the registration statement filed shortly thereafter and the actual value of the package appeared as soon as the exchange offer became effective. I therefore find it unnecessary to decide whether a reasonable investor would have construed the $80 promised value to refer to market price of the security or to an appraisal of BPC's assets and earnings, or whether the archetypical investor should have been expected to make this differentiation from the bare words of the press release.

I also concur in the majority view that CCI has not proved its claim based upon the letters sent by the Piper family to Piper shareholders in June and July, 1969. Although these letters failed to mention the arrangement with BPC whereby the Piper family might gain a huge profit if BPC succeeded in acquiring control of the Piper Company, CCI promptly furnished the essential information to all Piper stockholders on June 16, 1969, before the BPC tender offer became effective. In view of the latter communication no reasonable investor would have accepted BPC's tender offer, which went into effect on July 18, 1969, in reliance upon the Piper family letters.

I must dissent, however, from the majority's failure to accord similar treatment to the claim based on the earlier letters written by the Piper family to Piper stockholders on January 27 and 28, 1969, and to the January 29 press release. I agree that these letters and press release were materially misleading and that a reasonable investor would have considered them important in deciding whether to accept or reject CCI's cash tender offer. Under the *Mills-Ute* test positive proof of reliance was unnecessary to establish causation. However, proof of damages is a separate question and requires more. As the Supreme Court stated in *Mills* v. *Electric Auto-Lite, supra* at 388-89:

> "On the other hand, where, as here, the misleading aspect of the solicitation did not relate to terms of the merger, monetary relief might be afforded to the shareholders only if the merger resulted in a reduction of the earnings or earnings potential of their holdings. In short, *damages should be recoverable only to the extent that they can be shown.*" (Emphasis supplied)

Applying this principle, CCI must show that it suffered some resulting loss. This it has failed to do. In making the January cash tender offer it agreed to purchase up to 300,000 Piper shares if tendered by February 3, 1969, and the district court found that it was not seeking more. 304,606 shares were tendered and purchased by CCI. Thus CCI exceeded its goal. It got more shares than it agreed to buy. No loss was suffered. Indeed it publicly stated that the cash tender offer had been a success.

Although CCI reserved the right to purchase more than 300,000 shares, it did not have sufficient funds to purchase any significant amount in excess of 300,000. Nor had "financing for . . . shares in excess of 300,000 . . . been arranged. . . ." (Testimony of C. Leonard Gordon, CCI's Vice-President and General Counsel). It is true that Mr. Gordon testified that Burnham & Co. would have provided additional financing if more than 300,000 shares had been tendered. However, the record shows conclusively that CCI's chances of obtaining such a loan were negligible, due to a restrictive agreement in effect with its senior noteholders and the prohibitive cost of borrowing additional funds.

Under its agreement with its senior noteholders CCI had obligated itself not to have any unsecured current debt for bank loans in excess of a $15,000,000 revolving line of credit already obtained from the Philadelphia National Bank. The parties have stipulated that on February 3, 1969, the entire proceeds of this $15 million loan were re-

ceived by CCI and used by it to pay for Piper shares received by it on its January 24, 1969, cash tender offer, which closed on the same date the loan proceeds were received. (App. 825A). By February 4, 1969, CCI had purchased 540,000 shares of Piper stock at a cost in excess of $30,000,000. Its cash resources were virtually exhausted. Yet it did not seek waivers from its senior noteholders to permit additional borrowing. Indeed, the parties have further stipulated that no resolution authorizing CCI to borrow money or obtain credit from any other source to purchase Piper stock was ever sought or adopted. (App. 284A).

The reason for CCI's failure to seek additional loans was made clear by testimony of Mr. Woudhuysen, a partner of Burnham & Co., that the borrowing terms would have involved an 8¾% interest rate plus the issuance of 22,500 CCI warrants, exercisable at the market price of CCI common stock, for each million dollars borrowed on a two-year loan. Thus if CCI should borrow $20 million on such a two-year loan the total cost of the money, calculated according to a commonly accepted formula, would have been a staggering 43.11%!

In summary, having "shot its bolt" in the financial sense by early February 1969 CCI was thereafter relegated in its quest for control of Piper to the use of exchange offers. It was in no position to purchase for cash any appreciable amount of Piper shares over and above the 304,606 tendered in response to its initial cash offer. Indeed, although additional Piper shares were available in the market after the expiration date of CCI's tender offer, some at less than $65 per share,[3] CCI purchased only 9,100 shares between

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3 The Piper family January letters and press release regarding the Grumman transaction did not cause an increase in the market price of Piper shares. On the contrary the price declined from 64¼ per share on January 28 to 59⅝ on February 3.

February 3, 1969, and April 7, 1969, when the SEC advised it that such cash purchases during the pendency of its exchange offer (for which it had filed its Form S-1 with the Commission on February 27, 1969, to become effective May 15, 1969) would violate Rule 10b-6. The record further reveals that although Herbert Siegel, Chairman of the Board of CCI, knew as early as February, 1969, that Cornfeld's Fund of Funds Proprietary Fund, Inc. owned a large block of 78,600 Piper shares (later purchased by BPC), CCI made no effort to purchase it. Nor can CCI's lack of pursuit of the substantial Cornfeld block be attributed to a hypothesized desire to avoid the expense of searching out and purchasing small blocks of shares, as the main opinion suggests.

By March 19, 1969, when the Grumman deal collapsed, any possible effect of the Piper family's January 29, 1969, Grumman press release was completely dissipated, and by April 7, 1969, when the SEC took the position that further cash purchases were prohibited by Rule 10b-6, CCI could no longer claim that the January letters inhibited its purchase of Piper shares. By May 8, 1969, when BPC announced its tender package valued at $80, CCI could no longer contend that the Piper family's statement that Piper shares were worth more than $65 per share was misleading. Nor is the main opinion's fanciful assumption that the January letters "undoubtedly . . . influenced" Piper shareholders against accepting CCI's later *exchange* offer by casting a general pall of unfairness over CCI's reputation anything more than rank speculation.

Dogged by its inability to obtain financing that would have enabled it to purchase available Piper stock for cash in competition with BPC, CCI's efforts to obtain control by the cash offer route were doomed to failure. By the close of its second exchange offer on August 4, 1969, CCI owned 41% of Piper's outstanding shares as compared with

45% owned by BPC. Thereafter it was BPC's cash purchases in the open market of 100,614 shares, as compared with CCI's capacity to buy only 29,200 shares, that won control for BPC.

Thus there has been a complete failure to show that the Piper family's January letters and press release, which form the sole basis for the majority's decision holding liable the Piper family defendants, caused any damage to CCI. The record is clear that the Piper communications, unlike the misleading statements in BPC's exchange offer or BPC's cash purchases in violation of Rule 10b-6, did not deprive CCI of a fair opportunity to compete in the contest for control or enable BPC to win that contest.

In short, since the record shows that CCI did not suffer any damages as a result of the Piper family's communications, I would affirm the dismissal of CCI's claim against the members of that family.

First Boston and its Officers

Where an underwriter participates in an exchange offering by assisting in the preparation of the registration statement and prospectus and by lending its name to the offer, I agree that §14(e) should be construed to impose upon him the same obligation as that imposed upon the issuer with respect to materially false or misleading statements or omissions, and that a damage suit should lie against the underwriter in favor of the competing bidder for control who suffered resulting damage. This conclusion is based solely upon the principle of implying liability as a means of promoting private enforcement of the antifraud provisions of the securities laws. See pp. 2-4, *supra.* However, unlike the main opinion on this issue, I gain no assistance in reaching that decision from §11(b) of the 1933 Act, 15 U.S.C. §77k(b) or from the Senate Report

accompanying §14(e), S. Rep. No. 510, 90th Cong., 2d Sess. (1968).

Since §11(b) *expressly* creates liability for materially misleading statements in a prospectus and then only in favor of purchasers of the security, I fail to find it of any help in *implying* liability under §14(e) in favor of non-purchasers. Indeed it could be argued that the very fact that Congress expressly delineated the scope of liability in §11(b) militates against implying liability in §14(e). As for the Senate Report accompanying §14(e), I believe the authors would be startled to find that they had in mind underwriters such as First Boston Corp. when they referred generally to persons "engaged in making . . . tender offers or otherwise seeking to influence" the decision of investors with respect to such offers.

Injunctive Relief

I concur in the well-reasoned opinion of Judge Gurfein affirming the district court's denial of injunctive relief against violation by BPC of the Securities Act of 1933, 15 U.S.C. §77a, *et seq.*, and the Securities Exchange Act of 1934, 15 U.S.C. §78a, *et seq.* 331 F. Supp. 1154.

The dissent's description of BPC's conduct as "most flagrant," its characterization of the district court's action as an "abuse of discretion," and its portrayal of our decision as a "mischievous precedent," simply ignore undisputed contrary findings of fact, which are fully supported by more than ample credible evidence. Such comments sacrifice controlling evidence and governing legal principles to insatiable zeal for use of an unjustified remedy, all in the name of vigorous enforcement of federal securities laws.

A review of the claims, evidence and findings demonstrates the wisdom of allowing Judge Pollack's decision denying injunctive relief to stand. The Commission's claim

was that BPC's registration statement and prospectus were materially deficient because of an alleged failure to disclose that it had decided to sell BAR at a price some $13.4 million below the figure at which it was carried on BPC's financial statements, and that BPC deliberately deferred the closing of the sale until its exchange offer was completed in order to avoid making the writedown that would be required if the sale were completed prior to or during the pendency of the offer. After receiving extensive proof on these issues, including the testimony of key witnesses who were personally observed and whose credibility was appraised by Judge Pollack, whose experience in the field of securities litigation at least matches if not exceeds that of this panel, he found that during the period when BPC's registration statement and prospectus were in effect (i.e., from July 18, 1969 to August 27, 1969) no decision to sell had been made.[4] However he further found that although there was no intent to mislead on the part of BPC in carrying BAR at $18.4 million on the balance sheet, that figure was obsolete to the point of being misleading and should have been qualified by reference to pending negotiations for sale at a substantially lower figure.[5] These crucial

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4 "The Court has found that as of these dates Bangor Punta had not reached a decision to sell. The Commission's charge that the sale was a reasonable probability is made from the vantage point of hindsight. In the total perspective of events preceding the sale—including the last-minute attempts to convert it into a sale of assets—the Court cannot find that the sale was a reasonable probability at the time and to the people involved." (331 F. Supp. at 1160-61).

5 "The essential question is whether, despite the non-existence of intent or of reasonable probability, the circumstances surrounding the sale were such as to indicate that the $18.4 million carrying figure of the BAR holding was obsolete to the point of being misleading. The Court finds that it was—absent full disclosure of the factors affecting the ultimate decision to sell the BAR interest at a figure of $5 million—or even $7 million—and regardless of whether the sale was to be of stock or of assets.

* * * * *

findings, supported by substantial evidence, cannot be rejected by us.

> "Our court is not disposed to overturn conclusions of the trier of facts which are based upon substantial evidence and upon a determination of the credibility of witnesses who have given conflicting versions of the facts. N.L.R.B. v. Chain Service Restaurant Employees, 302 F.2d 167, 171 (2 Cir. 1962); Wilson v. United States, 229 F.2d 277, 279 (2 Cir. 1956); Phelan v. Middle States Oil Corp., 220 F.2d 593, 598 (2 Cir.), cert. denied sub nom. Cohen v. Glass, 349 U.S. 929, 75 S.Ct. 772, 99 L.Ed. 1260 (1955). Moreover, where a trial has been had by a judge without a jury, the judge's findings must stand unless 'clearly erroneous.' Fed.R.Civ.P. 52(a), 28 U.S.C." *Heyman* v. *AR. Winarick, Inc.*, 325 F.2d 584, 589 (2d Cir. 1963).

The dissent reluctantly concedes that the foregoing findings are supported by substantial evidence and confirms, in accordance with our decision in *SEC* v. *Manor Nursing Centers Inc.*, 458 F.2d 1082, 1100 (2d Cir. 1972), that in deciding whether to grant the extraordinary remedy of injunctive relief the district judge is vested with "broad discretion," which may be set aside only upon a clear showing of abuse of discretion. *United States* v. *W. T. Grant*

"I find that Bangor Punta did not intentionally or purposefully mislead Piper Aircraft stockholders or the investing public by the omission to make disclosure of the sale under consideration nor did Bangor Punta or its directors intend to gain an advantage over Chris-Craft by the nondisclosure in the contest being waged for control of Piper. There was no purposeful connection between the nondisclosure and the contest for control. In other words, the nondisclosure was not prompted by an improper purpose. However, absence of bad faith does not excuse the failure to include facts necessary to render the statements in the registration statement and prospectus not misleading." *SEC* v. *Bangor Punta Corp.*, 331 F. Supp. 1154, 1161 (S.D.N.Y. 1971).

Co., 345 U.S. 629, 633 (1953); *SEC* v. *Culpepper*, 270 F.2d 241, 249-50 (2d Cir. 1959); *SEC* v. *Torr*, 87 F.2d 446 (2d Cir. 1937); *SEC* v. *Okin*, 139 F.2d 87, 88 (2d Cir. 1943); *SEC* v. *Universal Service Ass'n*, 106 F.2d 232 (7th Cir.), *cert. denied*, 308 U.S. 622 (1939); *SEC* v. *Pearson*, 426 F.2d 1339 (10th Cir. 1970). However the dissent seeks to avoid these time-honored basic principles by suggesting that we may invoke a less stringent standard of review when the appeal is from *denial* of injunctive relief rather than from *grant* of such relief, relying upon *NMU* v. *Commerce Tankers Corp.*, 457 F.2d 1127 (2d Cir. 1972), which dealt with relief against unfair labor practices. That case is clearly distinguishable and has no application here. There we expressly noted that in deciding whether injunctive relief pending final adjudication by the NLRB in unfair labor practice cases is appropriate under 29 U.S.C. §160(1), "the role of the district court . . . is not to determine whether there has in fact been a violation of the Act but rather to determine whether the Regional Director could have *reasonable cause to believe* that the unfair labor practice charged had been committed and that its continuation ought to be enjoined." *Id.* at 1133 (emphasis in original). No such considerations control here, where a showing must be made that the person charged "is engaged or about to engage in any acts or practices which constitute or will constitute a violation," 15 U.S.C. §§77t(b), 78u(e).

We have found no instance where the standard for review of unfair labor practice suits has been applied to a suit by the SEC. On the contrary, in affirming the denial of injunctive relief in a suit by the SEC, the Tenth Circuit has taken the opposite view:

> "We are obliged to give great weight to the supported findings including the trial court's conviction that ap-

pellee did not intend further participation in the stock brokerage business in which he had not engaged for over a year before the hearing. See S.E.C. v. Franklin Atlas Corporation, supra 171 F. Supp. at 718. While we are persuaded that certain findings were clearly erroneous, we cannot say that there is a showing of abuse of the trial court's discretion in denial of the preliminary injunction and affirm that ruling." *SEC* v. *Pearson,* 426 F.2d 1339, 1344 (10th Cir. 1970).

With respect to the contention that Judge Pollack applied an erroneous standard in determining whether an injunction should issue, we would be engaging in petty semanticism if we were to reverse his decision because of his use of the words "propensity or natural inclination" instead of the phrase "reasonable likelihood that the wrong will be repeated." There is nothing magic about either phrase, as was recognized in *SEC* v. *Manor Nursing Centers, Inc.,* 458 F.2d 1082, 1101 (2d Cir. 1972), where this court, referring to Judge Pollack's use in this very case of the terms "propensity or natural inclination to violate the securities laws," said: "In relying upon our decision in *Texas Gulf Sulphur,* which applied the reasonable likelihood standard, the district court demonstrated that it was not purporting to apply a new standard for the issuance of an injunction." I am not persuaded by the dissent's present attempt to explain away this earlier view of the standard adopted by Judge Pollack. Although there is a slight difference between the two clauses, both express substantially the fundamental condition precedent to the issuance of the extraordinary remedy of a permanent injunction, i.e., that there must be a showing of a cognizable risk of future violation, something "more than the mere

possibility which serves to keep the case alive." *United States* v. *W.T. Grant Co.*, 345 U.S. 629, 633 (1953).[6]

Nor was injunctive relief denied merely because of lack of wrongful intent. Judge Pollack expressly recognized (*supra* n.5) that absence of bad faith or of an intent or purpose to violate the securities laws will not necessarily excuse the defendant and that an evil intent need not be shown to grant relief. But the lack of such intent is an important factor to be considered by the court in assessing the risk of future violations. One who intentionally violates the law or shows a willful disregard for it is usually a poorer risk than one who acts without a full appreciation for the seriousness of his conduct. In addition, however, the court must weight all of those considerations which have been the traditional concern of the courts of equity, including the nature and extent of past violations, the effect on the public interest, and the impression on the trial judge made by the defendants who testified. *SEC* v. *Harwyn Industries Corp.*, 326 F. Supp. 943, 955-58 (S.D.N.Y. 1971).

The $18.4 million ascribed to BAR as "stated book value" on BPC's financial statements was an obsolete and hence misleading figure in view of pending negotiations for sale of the railroad at a much lower price. Some caveat or reference to the negotiations was required. However, I cannot agree that BPC's failure to furnish additional data was "flagrant." This characterization ignores the fact that under generally accepted accounting principles "stated book value" may properly be used in a financial statement

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6 It appears to have been the SEC in its brief that first used the phrase adopted by Judge Pollack, "Because of this demonstrated propensity for violating the securities laws, the scope of the injunction against Bangor Punta should be broad," etc. Brief, p. 16, citing *SEC* v. *Raffer*, 1969-1970 CCH Fed.Sec.L.Rep. ¶92,632 (S.D.N.Y. 1970). It was this standard put forward by the Commission to which Judge Pollack was evidently responding below. 331 F. Supp. at 1162-63.

and is not viewed in the financial world as the equivalent of market value. A person able to read a balance sheet would probably have recognized that such "historical" cost did not necessarily represent current liquidating value. Furthermore, to write down the figure immediately to $5 million might have been treated by the SEC as speculative and possibly misleading, in view of the other forms of disposition of BAR that were still under consideration.

The other alleged "past violation" chargeable against BPC—that its May 8, 1969 press release constituted an offer to sell before any registration statement had been filed—constituted at most a technical violation. BPC filed its registration statement and preliminary prospectus shortly after the May 8th release and in consenting to a permanent injunction it did not admit any of the allegations of the complaint filed against it in the District Court for the District of Columbia.

Nor can I agree that BPC should be singled out for special injunctive treatment because it is a conglomerate. There is no evidence to support the view that it has "long been interested in new acquisitions" or that it will "become involved in similar tender offers in the future." We are not concerned here with a corporate behemoth of the size of ITT but with a corporate venture of relatively modest size. Even if BPC should become interested in further lawful acquisitions for what it conceives to be sound economic reasons, the totality of the circumstances do not indicate any likelihood that it will engage in further violations of the securities acts.

Aside from the foregoing factors I am convinced that a judgment which (1) awards compensatory damages to CCI, (2) bars BPC from voting its illegally acquired Piper shares, and (3) awards rescission to former Piper stockholders who exchanged their shares in response to BPC's tender offer, amply protects the public interest and insures

against any reasonable likelihood that BPC will engage in similar conduct in the future.

The relief granted is bitter medicine which will be far more effective than a blanket injunction in deterring infraction of the law.

APPENDIX I

Order of Second Circuit Court of Appeals, Denying Petition for Rehearing, dated April 25, 1973

Order Denying Petition for Rehearing

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

Docket No. 72-1064

CHRIS-CRAFT INDUSTRIES, INC.,

Plaintiff-Appellant,

v.

PIPER AIRCRAFT CORPORATION, HOWARD PIPER, THOMAS F. PIPER, WILLIAM T. PIPER, JR., BANGOR PUNTA CORPORATION, NICOLAS M. SALGO, DAVID W. WALLACE, THE FIRST BOSTON CORPORATION, PAUL L. MILLER and NICHOLAS H. BAYARD,

Defendants-Appellees.

ORDER

Petitions for rehearing having been filed herein on March 30, 1973 on behalf of appellees Howard Piper, Thomas F. Piper and William T. Piper, Jr.; on behalf of appellees Bangor Punta Corporation, Nicolas M. Salgo and David W. Wallace; and on behalf of appellees The First Boston Corporation, Paul L. Miller and Nicholas H. Bayard; and

Due consideration by the undersigned members of the panel having been given to said petitions for rehearing; it is therefore

Order Denying Petition for Rehearing

ORDERED as follows:

(1) That, with respect to the petition for rehearing on behalf of appellees Paul L. Miller and Nicholas H. Bayard, the said petition is granted to the extent that the main opinion filed herein on March 16, 1973 is amended by adding the following sentence at the end of the first paragraph concluding on slip opinion page 4965, line 12:

> "In view of the voluminous record, upon remand, the district court shall determine from the record whether, under the principles of liability regarding First Boston and its officers in this opinion, Paul L. Miller and Nicholas H. Bayard, or either of them, is individually liable."

(2) That in all other respects the said petitions for rehearing are denied.

Dated at New York, N.Y. this 25th day of April, 1973.

WALTER R. MANSFIELD

WALTER S. MANSFIELD
United States Circuit Judge

WM H. TIMBERS

WILLIAM H. TIMBERS
United States Circuit Judge

MURRAY I. GURFEIN

MURRAY I. GURFEIN
United States District Judge

APPENDIX J

Orders of Second Circuit Court of Appeals, Denying Petition for Rehearing, *in banc*, dated April 25, 1973

J-1

Order Denying Petition for Rehearing in banc

UNITED STATES COURT OF APPEALS

SECOND CIRCUIT

At a Stated Term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Court House, in the City of New York, on the twenty-fifth day of April, one thousand nine hundred and seventy-three.

CHRIS-CRAFT INDUSTRIES, INC.,

Plaintiff-Appellant,

v.

PIPER AIRCRAFT CORPORATION, HOWARD PIPER, THOMAS F. PIPER, WILLIAM T. PIPER, JR., BANGOR PUNTA CORPORATION, NICHOLAS M. SALGO, DAVID W. WALLACE, THE FIRST BOSTON CORPORATION, PAUL L. MILLER and NICHOLAS H. BAYARD,

Defendants-Appellees.

A petition for a rehearing containing a suggestion that the action be reheard in banc having been filed herein by counsel for the appellees, The First Boston Corporation, et al., and no active circuit judge having requested that a vote be taken on said suggestion,

Upon consideration thereof, it is

Ordered that said petition be and it hereby is denied.

A. DANIEL FUSARO, *Clerk*

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Order Denying Petition for Rehearing in banc

UNITED STATES COURT OF APPEALS

SECOND CIRCUIT

At a Stated Term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Court House, in the City of New York, on the twenty-fifth day of April, one thousand nine hundred and seventy-three.

CHRIS-CRAFT INDUSTRIES, INC.,

Plaintiff-Appellant,

v.

PIPER AIRCRAFT CORPORATION, HOWARD PIPER, THOMAS F. PIPER, WILLIAM T. PIPER, JR., BANGOR PUNTA CORPORATION, NICHOLAS M. SALGO, DAVID W. WALLACE, THE FIRST BOSTON CORPORATION, PAUL L. MILLER and NICHOLAS H. BAYARD,

Defendants-Appellees.

A petition for a rehearing containing a suggestion that the action be reheard in banc having been filed herein by counsel for the appellees, Bangor Punta, et al., and no active circuit judge having requested that a vote be taken on said suggestion,

Upon consideration thereof, it is

Ordered that said petition be and it hereby is denied.

A. DANIEL FUSARO, *Clerk*

J-3

Order Denying Petition for Rehearing in banc

UNITED STATES COURT OF APPEALS

SECOND CIRCUIT

At a Stated Term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Court House, in the City of New York, on the twenty-fifth day of April, one thousand nine hundred and seventy-three.

CHRIS-CRAFT INDUSTRIES, INC.,

Plaintiff-Appellant,

v.

PIPER AIRCRAFT CORPORATION, HOWARD PIPER, THOMAS F. PIPER, WILLIAM T. PIPER, JR., BANGOR PUNTA CORPORATION, NICOLAS M. SALGO, DAVID W. WALLACE, THE FIRST BOSTON CORPORATION, PAUL L. MILLER and NICHOLAS H. BAYARD,

Defendants-Appellees.

A petition for a rehearing containing a suggestion that the action be reheard in banc having been filed herein by counsel for the appellees, Piper, et al., and no active circuit judge having requested that a vote be taken on said suggestion,

Upon consideration thereof, it is

Ordered that said petition be and it hereby is denied.

A. DANIEL FUSARO, *Clerk*